Supreme Court, U.S.
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No. 01-

IN THE
Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PENNSYLVANIA,
Petitioner,

v.

TEXTRON FINANCIAL CORPORATION,
Respondent.

**Petition for a Writ of Certiorari
to the Court of Appeal of California,
Fourth Appellate District**

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Should this Court grant the petition, vacate the judgment below, and remand for further consideration in light of the intervening decision in *Cooper Industries, Inc.* v. *Leatherman Tool Group, Inc.*, 121 S. Ct. 1678 (2001), which held that a court of appeals must review *de novo* a judgment awarding punitive damages?

PARTIES TO THE PROCEEDINGS AND RULE 29.6 STATEMENT

Petitioner National Union Fire Insurance Company of Pittsburgh, Pennsylvania, was the defendant, appellant, and cross-appellee below. Respondent Textron Financial Corporation was the plaintiff, appellee, and cross-appellant below. Petitioner is wholly owned by American International Group, Inc., and has one non-wholly-owned subsidiary, JI Accident & Fire Insurance Co., Ltd. (Japan).

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**Petition for a Writ of Certiorari
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PETITION FOR A WRIT OF CERTIORARI

National Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union") respectfully petitions for a writ of certiorari to review the judgment of the Court of Appeal of California, Fourth Appellate District, in this case.

OPINIONS BELOW

The January 29, 2001, Opinion of the Court of Appeal of the State of California, Fourth Appellate District, Division Three is unreported and reproduced in the appendix hereto ("App.") at 1a. The May 29, 1996, Judgment of the Superior Court of the State of California, Orange County, is unreported and reproduced at App. 26a. The July 29, 1996, Order

of the Superior Court conditionally granting a new trial is unreported and reproduced at App. 36a. The May 2, 2001, Order of the Supreme Court of California denying National Union's petition for review is unreported and reproduced at App. 43a. The May 4, 2001, Order of the Supreme Court of California correcting a clerical error in its earlier Order is unreported and reproduced at App. 44a.

JURISDICTION

The judgment of the Court of Appeal was entered on January 29, 2001. On May 2, 2001, the Supreme Court of California denied National Union's timely petition for review. App. 43a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISION INVOLVED

The Fourteenth Amendment to the United States Constitution provides, in pertinent part: "No State shall * * * deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV, sec. 1.

INTRODUCTION

Petitioner National Union appealed a $1.7 million punitive damages award to the California Court of Appeal, arguing that the award was excessive and violated National Union's right to due process under the Fourteenth Amendment to the United States Constitution. The Court of Appeal affirmed the award after declaring that the judgment below was "presumed to be correct" and reviewing the record "most favorably to the judgment." App. 24a. National Union petitioned the Supreme Court of California to review the decision, arguing that the Court of Appeal had failed to conduct a *de novo* review of the trial court's judgment to ensure that the punitive damages award comported with the Fourteenth Amendment. The Supreme Court of California denied National Union's petition without comment.

Twelve days after the Supreme Court of California denied review, this Court issued *Cooper Industries, Inc.* v. *Leatherman Tool Group, Inc.*, 121 S. Ct. 1678, 1685-86 (2001), holding that "courts of appeals should apply a *de novo* standard of review when passing on district courts' determinations of the constitutionality of punitive damages awards." As it has done once already with a decision from the California Court of Appeal, this Court should grant certiorari, vacate the decision of the Court of Appeal in this case, and remand to allow the court to consider this case in light of the intervening decision in *Cooper Industries*.

STATEMENT OF THE CASE

Background.

This $1.7 million punitive damages case arises out of a claim for damage to a bus. In 1992, Il Sung Ko, the operator of a Los Angeles tour company, sought to purchase an insurance policy covering his fleet of buses. Through Douglas Ferguson, an independent insurance broker, Ko obtained a National Union insurance policy issued by TRM International ("TRM"), an independent company acting as a "managing general agent" for National Union.[1] Respondent Textron Financial Corporation ("Textron") had a security interest in one of Ko's buses and was named as loss payee on the National Union insurance policy. The "loss payable" endorsement on the policy specified that if National Union were to cancel the policy, Ko and Textron would receive "the same advance notice."

After he purchased the National Union policy, Ko's financial situation declined, and he purportedly stopped using two of his buses, including the bus financed by Textron. Ferguson advanced Ko several thousand dollars in insurance premiums during that time. In late 1992, when Ko was

[1] The term "managing general agent" is a term of art in the insurance field; it describes a company that markets and issues insurance policies on behalf of insurance companies pursuant to an agency agreement.

unable to pay Ferguson back and after National Union threatened to cancel Ko's policy, Ko and Ferguson requested that TRM delete coverage of the two supposedly idle buses and issue a "premium credit" for the deleted vehicles. The deletion endorsement negotiated by the parties in late 1992 staved off cancellation of Ko's entire policy and enabled him to operate the rest of his fleet; in addition, Ferguson testified that the accompanying refund in the form of a premium credit would have repaid him for the substantial amount of money he had fronted to Ko. TRM prepared an endorsement to the policy stating that coverage for the bus had been deleted. Although TRM's records indicate that a copy of the endorsement was mailed to Textron, Textron denied receiving it. [2]

Ko continued to use the Textron-financed bus despite claiming to have garaged it, and in January 1993, the bus was involved in an accident. Ferguson notified the American International Adjustment Company ("AIAC")—a company affiliated with National Union and vested with authority to investigate, approve, defend, or deny claims by or against National Union insureds—that the accident had occurred, and that Ko had previously requested the bus be deleted from the policy. A TRM supervisor confirmed Ferguson's statement, and AIAC accordingly informed Ko that coverage would be denied.

Textron learned about the accident—and the deletion from the policy of the bus it had financed—several months later, after Ko defaulted on his loan obligations. Textron sued Ko for the balance due on the loan and secured a judgment against him, which Ko subsequently discharged in a bankruptcy proceeding. Textron also submitted a claim to National Union for $61,000 in property damage. After a lengthy investigation, National Union denied Textron's

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[2] The deletion endorsement was effective as of December 1, 1992, but was not generated until February 1993. According to TRM, the delay was attributable to a backlog in administrative paperwork.

claim, concluding that it was not obligated under the policy to notify Textron of the cancellation by Ko.

Textron then sued National Union and AIAC, alleging breach of contract, breach of the covenant of good faith and fair dealing, conspiracy, and fraud.[3] Textron's contract claims were based on the parties' dispute over whether the loss payable endorsement required National Union to provide a lienholder with advance notice if a vehicle was deleted at the insured's request. Textron's conspiracy and fraud claims were grounded in a more sinister theory, however: that in fact the bus had not been deleted from the policy before the accident. According to Textron, following the accident, various TRM employees had engaged in a complicated "post-accident underwriting" scheme to mislead Textron into believing that coverage for the bus had been canceled before the accident, when in fact the bus was subject only to a "lay up credit"—a procedure sometimes used by a commercial insured with a fleet of vehicles who experiences a temporary lull in business. Under a lay up credit, coverage remains in effect, but the insurer provides a credit for the period of time the vehicle temporarily is out of service. Textron further claimed that TRM officials had fabricated various documents to support its position that the bus had been deleted from the policy, and that National Union and AIAC had subsequently ratified TRM's deception by vigorously defending the coverage denial. According to Textron, the purpose of this intrigue was to deny Textron—which paid National Union millions of dollars a year in insurance premiums—a $61,500 property damage claim.

At trial, the court ruled that National Union could not terminate Textron's rights as a loss payee without advance notice to Textron. Textron's contract damages claim, its claim for insurance bad faith, and its fraud and conspiracy

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[3] Textron also brought claims against National Union and AIAC under California's unfair business practices statute. Those claims were dismissed prior to trial. In the same complaint, Textron also sued TRM and Ferguson for negligence. Both settled before trial.

claims were then tried to a jury, which found National Union liable for the money payable under the insurance policy. App. 27a. The jury also concluded that National Union had committed insurance bad faith, rendering the company liable for approximately $86,000 in attorney's fees and costs incurred by Textron to prosecute this action. App. 34a. The jury further concluded that AIAC had not made misrepresentations knowingly or with an intent to defraud, but that National Union had made such representations. App. 29a-30a. The jury awarded Textron $3,859.50 in compensatory damages on its fraud claim, representing the legal fees incurred when, relying on National Union's purported misstatements that coverage had been deleted, Textron pursued Ko for damages. App. 31a. The jury then awarded Textron $10 million in punitive damages against National Union. App. 34a.

On National Union's motion, the Superior Court granted a conditional new trial, unless Textron agreed to a remittitur of the punitive damage award to $1.7 million. App. 40a. Textron accepted the remittitur, App. 41a-42a, and National Union appealed.[4]

The Decision of the California Court of Appeal.

On appeal, National Union argued that even with the trial court's remittitur, $1.7 million in punitive damages was excessive and violated National Union's right to due process under the Fourteenth Amendment to the United States Constitution. National Union explained that the three "guideposts" set forth by this Court in *BMW of North America, Inc.* v. *Gore*, 517 U.S. 559, 575-585 (1996)—the reprehensibility of the defendant's conduct, the ratio of punitive damages to the plaintiff's actual harm, and comparable civil or criminal penalties arising from the same conduct—mandated a finding that the trial court had erred in awarding Textron a colossal sum in punitive damages on a

[4] Textron filed a cross-appeal, claiming, among other things, that the trial court erred in granting the remittitur.

claim for a small fraction of that amount. Addressing each *BMW* factor at length, National Union argued that the trial court's punitive damages award constituted an "arbitrary deprivation of property" in violation of the Fourteenth Amendment's due process clause. *See Honda Motor Co.* v. *Oberg*, 512 U.S. 415, 430 (1994).

The Court of Appeal affirmed. App. 1a, 25a. Citing its decision in *Stevens* v. *Owens-Corning Fiberglas Corp.*, 57 Cal. Rptr. 2d 525 (Cal. Ct. App. 1996), the court announced that "[o]n appeal, a judgment awarding punitive damages *is presumed to be correct* and will be reversed only if the record, *viewed most favorably to the judgment*, reflects the award is the result of passion or prejudice." App. 24a (emphases added). Observing only that "the evidence reflects National Union engaged in reprehensible conduct" and that "the award necessarily had to be large to affect a corporate entity such as National Union," the Court of Appeal concluded that the $1.7 million punitive damages award was "not excessive, nor does it violate National Union's constitutional right to due process of law." App. 25a.

Following the Court of Appeal's decision, National Union filed a petition for review in the Supreme Court of California, arguing that the appellate court had failed to "conduct an independent review of the size of a punitive damage award" to ensure the award conformed with the Fourteenth Amendment. Pet. for Review 1. Citing (among other cases) *Ornelas* v. *United States*, 517 U.S. 690, 697 (1996) and *Haynes* v. *Washington*, 373 U.S. 503, 515 (1963), National Union argued that the United States Supreme Court had consistently held that review of constitutional claims should be *de novo*, but that the Court of Appeal had taken a far more permissive approach.

Indeed, the Court of Appeal had failed entirely to examine the three factors identified in *BMW* v. *Gore*. The court

concluded that National Union's conduct was "reprehensible"—a precursor to any punitive damages award—but did not determine to what degree National Union's conduct was reprehensible. *See BMW*, 517 U.S. at 575. The court concluded that the damages award "had to be large" to affect National Union, App. 24a, and that "no fixed ratio exists to determine the proper proportion between" compensatory and punitive damages, *id.* at 25a, but it did not determine whether a $1.7 million judgment was excessive when compared to Textron's comparatively minimal damages. *See BMW*, 517 U.S. at 582-583. And it failed to consider analogous civil and criminal penalties for similar acts. *See id.* at 583-584. National Union explained that the Court of Appeal had completely abdicated its obligation to independently examine whether the punitive damage award passed constitutional muster by essentially rubber-stamping the trial court's decision. The Supreme Court of California denied review without comment on May 2, 2001. App. 43a.

Cooper Industries.

Less than two weeks after the Supreme Court of California denied review, this Court decided *Cooper Industries, Inc.* v. *Leatherman Tool Group, Inc.*, 121 S. Ct. 1678 (2001). Reviewing a case from the Ninth Circuit, this Court held that "courts of appeals should apply a *de novo* standard of review when passing on district courts' determinations of the constitutionality of punitive damages awards." 121 S. Ct. at 1685-86.

This Court explained that the Fourteenth Amendment's due process clause imposes "substantive limits" on States' discretion to punish by prohibiting States from imposing "grossly excessive" deprivations of life, liberty or property. *Id.* at 1684. In reviewing excessive punishment cases, this Court stated, it had routinely engaged in an "independent examination of the relevant criteria" informing a ruling on excessiveness: the degree of the defendant's culpability; the

"relationship between the penalty and the harm to the victim;" and the "sanctions imposed in other cases for comparable misconduct." *Id.* at 1684-85.

This Court noted that in *United States* v. *Bajakajian*, 524 U.S. 321 (1998), which held that a punitive forfeiture of approximately $350,000 for violating a reporting requirement was grossly disproportional to the offense, it had specifically stated that "courts of appeals must review the proportionality determination '*de novo*'," rejecting respondent's argument that the trial court's ruling on excessiveness should be reviewed for abuse of discretion. *Cooper Industries*, 121 S. Ct. at 1685 (quoting *Bajakajian*, 524 U.S. at 336-337 n.10). This Court had applied the same standard in *Ornelas*, 517 U.S. at 696, holding that a trial court's determinations on reasonable suspicion and probable cause should be examined *de novo* by a reviewing court. *See Cooper Industries*, 121 S. Ct. at 1685.

Because punitive damage awards, like the determinations in *Bajakajian* and *Ornelas*, implicate constitutional questions, this Court held that reviewing courts must apply a *de novo* standard of review when assessing the constitutionality of punitive damage awards. *Id.* at 1685-86. The Ninth Circuit had applied a less exacting standard, reviewing the district court's punitive damages ruling for abuse of discretion. *Id.* at 1682. This Court accordingly vacated the judgment and remanded. *Id.* at 1689.

REASON FOR GRANTING THE WRIT

THE DECISION BELOW WAS RENDERED PRIOR TO, AND CONFLICTS WITH, THIS COURT'S DECISION IN *COOPER INDUSTRIES*.

This Court issued its decision in *Cooper Industries* twelve days after the Supreme Court of California denied National Union's petition for review of the decision of the Court of Appeal. Certiorari should be granted and the Court of

Appeal's decision vacated and remanded for consideration in light of *Cooper Industries*.

1. This Court will grant certiorari, vacate a judgment, and remand ("GVR") when it concludes that intervening precedent is "sufficiently analogous and, perhaps, decisive to compel re-examination of the case." *Henry* v. *City of Rock Hill*, 376 U.S. 776, 777 (1964). "Where intervening developments * * * reveal a reasonable probability that the decision below rests upon a premise that the lower court would reject if given the opportunity for further consideration, and where it appears that such a redetermination may determine the ultimate outcome of the litigation, a GVR order is * * * potentially appropriate." *Lawrence* v. *Chater*, 516 U.S. 163, 167 (1996) (per curiam).[5] As this Court has explained, "a GVR order both promotes fairness and respects the dignity of the Court of Appeals by enabling it to consider potentially relevant decisions and arguments that were not previously before it." *Stutson* v. *United States*, 516 U.S. 193, 197 (1996). A GVR order is warranted here, because the California Court of Appeal clearly applied the standard disapproved by *Cooper Industries* when it reviewed the punitive damages judgment.

When it reviewed the constitutionality of the trial court's punitive damage award, the Court of Appeal stated that "a judgment awarding punitive damages is *presumed to be correct*," and that the award would be reversed "only if the

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[5] For example, following its decision in *Pacific Mutual Life Ins. Co.* v. *Haslip*, 499 U.S. 1, 20 (1991), which stressed the importance of "meaningful and adequate review" of juries' punitive damages determinations, this Court granted, vacated, and remanded several decisions of the California Court of Appeal for consideration in light of *Haslip*. *See Transamerica Occidental Life Ins. Co.* v. *Koire*, 500 U.S. 950 (1991); *AMCA Int'l Fin. Co.* v. *Hilgedick*, 499 U.S. 972 (1991); *Pacific Lighting Corp.* v. *MGW, Inc.*, 499 U.S. 915 (1991); *Church of Scientology* v. *Wollersheim*, 499 U.S. 914 (1991); *International Soc. of Krishna Consciousness* v. *George*, 499 U.S. 914 (1991).

record, *viewed most favorably to the judgment*, reflects the award is the result of passion or prejudice." App. 24a (emphases added). That is a strange admixture of standards of review; but the one certain thing is that the Court of Appeal's review was not *de novo*. "Presum[ing]" the punitive damage award to be correct smacks of the typical standard of appellate review of certain factual findings. *See, e.g.*, *Summer* v. *Mata*, 449 U.S. 539, 550 (1981) (state court factual findings presumed to be correct for purposes of federal habeas review); *compare Cooper Industries*, 121 S. Ct. at 1686 (concluding that "the jury's award of punitive damages does not constitute a finding of 'fact' "). And to view the record "most favorably to the judgment" awarding punitive damages means to accord the lower court's decision deference—deference this Court has since found inappropriate in reviewing the constitutionality of a punitive damages award. Of course, a court of appeals reviews *de novo* a grant of summary judgment by viewing the record in the light most favorable to the *nonmovant*—the same standard the trial court applies. *See United States* v. *Diebold*, 369 U.S. 654, 655 (1962). But that is far different than reviewing the record "most favorably to the *judgment*;" that standard requires deference to the original decisionmaker, and is inappropriate after *Cooper Industries*.

2. As support for its standard of review, the Court of Appeal cited *Stevens* v. *Owens-Corning Fiberglas Corp.*, 57 Cal. Rptr. 2d 525 (Cal. Ct. App. 1996). That case confirms that the Court of Appeal misperceived its role. *Stevens* held that when determining whether a punitive damages award is excessive, "[a]ll presumptions favor the correctness of the verdict and judgment," and that while the "trial court's approval of the punitive damage award * * * is not binding on appeal, * * * we must give it significant weight." *Id.* at 533. The Court of Appeal's statement in this case that the lower court's verdict was "presumed to be correct" was

drawn directly from the deferential *Stevens* standard of review.

This case and *Stevens* are not aberrations; the California appellate courts have consistently endorsed the deferential standard of review employed in those cases. In *Bertero* v. *National General Corp.*, 529 P.2d 608, 624 n.12 (Cal. 1974), for example, the Supreme Court of California announced that it would continue to apply the "historically honored standard of reversing as excessive only those judgments which the entire record, when viewed most favorably to the judgment, indicates were rendered as the result of passion and prejudice." In *Neal* v. *Farmers Ins. Exchange*, 582 P.2d 980, 986 (Cal. 1978), as in this case, the trial court conditionally granted defendants' motion for new trial unless the plaintiff consented to a remittitur. The defendant challenged the punitive damages award remaining after remittitur, and the California Supreme Court affirmed the lower court's damages award after an "examination of the whole record in the light most favorable to the judgment." *Id.* And in *Fortman* v. *Hemco*, 259 Cal. Rptr. 311, 322 (Cal. Ct. App. 1989), the Court of Appeal expressly stated that when a reviewing court examines whether an award of punitive damages was excessive, "*it does not act de novo.*" (Emphasis added.) Rather, that court explained, the trial court's determination is " 'entitled to great weight,' " with "all presumptions favor[ing] the trial court's determination," and the court must "review the record in the light most favorable to the judgment." *Id.* (quoting *Hilliard* v. *A.H. Robins Co.*, 196 Cal. Rptr. 117, 144 n.28 (1983)). *See also Devlin* v. *Kearny Mesa AMC/Jeep/Renault, Inc.*, 202 Cal. Rptr. 204, 211 (Cal. Ct. App. 1984) (reviewing punitive damages award in "light most favorable to the judgment").

Similarly, other California decisions have upheld a punitive damages award if it is "supported by substantial evidence." *Shade Foods, Inc.* v. *Innovative Prods. Sales & Mktg., Inc.*, 93 Cal. Rptr. 2d 364, 395 (Cal. Ct. App. 2000), *citing*

National Auto. & Cas. Co. v. *Industrial Accident Comm'n*, 206 P.2d 841 (Cal. 1949); *Patrick* v. *Maryland Cas. Co.*, 267 Cal. Rptr. 24, 30 (Cal. Ct. App. 1990). As the *Shade Foods* court put it, substantial evidence review requires the court to " 'consider the evidence in the light most favorable to the prevailing party, giving him the benefit of every reasonable inference, and resolving conflicts in support of the judgment.' " 93 Cal. Rptr. 2d at 395 (quoting 9 Witkin, Cal. Procedure § 359, at 408 (4th ed. 1997)). The "substantial evidence" formulation of the California standard of review of punitive damages awards is equally suspect after *Cooper Industries*. *See San Paolo U.S. Holding Co.* v. *Simon*, 121 S. Ct. 2190 (2001) (granting certiorari, vacating, and remanding to California Court of Appeal for consideration in light of *Cooper Industries*).

3. It has not gone unnoticed that California's deferential standard of review lags behind the times. As one California Supreme Court justice recently observed, the deferential standard regularly employed by the courts of that State inhibits appellate courts "in providing guidance to trial courts as to how their broad discretion should be exercised. * * * [W]ithout clear guidance, judicial oversight of punitive damage awards will not be uniform, and the resulting gross variability in awards will ultimately implicate the rights of defendants to due process and the equal protection of the laws." *Lane* v. *Hughes Aircraft Co.*, 993 P.2d 388, 398 (Cal.) (Brown, J., concurring), *cert. denied*, 121 S. Ct. 307 (2000). That statement, which echoed this Court's observation in *Ornelas* that *de novo* review of constitutional determinations was necessary to "unify precedent and stabilize the law," 517 U.S. at 697-698, presaged as well this Court's statements to the same effect in *Cooper Industries*. *See* 121 S. Ct. at 1685 (citing *Ornelas*, 517 U.S. at 697-698 and *BMW*, 517 U.S. at 587).

4. Remand is particularly warranted here because, as in *Cooper Industries*, a "thorough, independent review" of the

punitive damages award "might well have led the Court of Appeals to reach a different result." 121 S. Ct. at 1688.

The first factor enumerated by this Court in *BMW*, and "[p]erhaps the most important indicium of the reasonableness of a punitive damages award," is the "degree of reprehensibility of the defendant's conduct." 517 U.S. at 575. The Court of Appeal remarked only that National Union's conduct was "reprehensible," App. 24a; but *BMW* of course requires a court to examine the *degree*, not just the fact, of reprehensibility, in order to pass on the appropriateness of a punitive damages award. The Court of Appeal based its decision affirming the punitive damage award on National Union's purported responsibility for the conduct of its independent agent TRM, expressly declining to decide whether National Union's own conduct, which consisted merely of verifying and defending its coverage decision, supported the punitive damages award. Even if National Union was appropriately held responsible for TRM's actions—a hotly disputed question below—National Union's derivative culpability pales in comparison with that of TRM itself, which settled with Textron for an amount equaling a tiny fraction of the punitive damages leveled against National Union. The conduct for which National Union was held liable caused purely economic harm, *see BMW*, 517 U.S. at 576, was not shown to be a part of any larger pattern of deceitful post-accident underwriting, *id.* at 576-577, and National Union's purported victim was in no sense "vulnerable," but a sophisticated company. *Id.* at 576.

Similarly, if the Court of Appeal had examined the ratio of punitive damages to the actual harm inflicted on Textron, rather than just asserting that National Union was "wealth[y]," App. 24a, the court might have reached a far different conclusion. This Court explained in *Pacific Mutual Life Ins. Co.* v. *Haslip* that a punitive award of "more than 4 times the amount of compensatory damages [and] more than 200 times the out-of-pocket expenses of respondent" was

"close to the line" of constitutional impropriety. 499 U.S. at 23. The ratio between the $1.7 million punitive damages award and the total damages awarded to Textron as a result of National Union's purported fraud and bad faith—just $3,860 in out-of-pocket damages plus $86,000 in attorney's fees awarded under California law—is nearly 20 to 1. Indeed, even including the damages under Textron's contract claim, which did not give rise to the punitive award, the ratio of punitive to total damages *still* exceeded 10 to 1.

Finally, the third *BMW* factor requires an inquiry into the statutory penalty for comparable acts. The Court of Appeal did not examine that factor at all; if it had, it would have found that the maximum statutory penalty established for insurance bad faith is $10,000. Cal. Ins. Code § 790.035. The huge disparity between that statutory sanction and the punitive damage award also justifies a finding that the award violated due process.

5. Finally, this Court has already granted certiorari, vacated, and remanded a decision of the California Court of Appeal following *Cooper Industries*. *See San Paolo U.S. Holding Co.* v. *Simon*, 121 S. Ct. 2190 (2001). In that case, the Court of Appeal affirmed a judgment granting the plaintiff $1.7 million in punitive damages (coincidentally, the same amount at issue here) by "view[ing] the entire record for substantial evidence from which the jury could reasonably conclude that the acts of San Paolo reached the level of reprehensibility to justify the award." *Simon* v. *San Paolo U.S. Holding Co.*, No. B121917 (reprinted in *San Paolo*, No. 00-1457, Pet. App. A-31). Stating that "an appellate court's task * * * 'begins and ends with a determination as to whether there is any substantial evidence, contradicted or uncontradicted, which will support the conclusion reached by the jury,' " the Court of Appeal in *Simon* concluded that it would not disturb the trial court's ruling. *San Paolo* Pet. App. A-32 (quoting *Crawford* v. *Southern Pacific Co.*, 45 P.2d 183, 184 (1935)).

San Paolo petitioned for certiorari, noting that the Court of Appeal's decision raised the question then pending before this Court in *Cooper Industries*. Pet. for Cert. (No. 00-1457) at 18-19. This Court granted, vacated, and remanded the decision for consideration in light of *Cooper Industries*. 121 S. Ct. 2190. It should do the same here.

CONCLUSION

For the foregoing reasons, the petition should be granted, the judgment below vacated, and the case remanded for further consideration in light of *Cooper Industries* v. *Leatherman Tool Group*.

Respectfully submitted,

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APPENDIX A

NOT TO BE PUBLISHED

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA
FOURTH APPELLATE DISTRICT
DIVISION THREE

G020323
(Super. Ct. No. 734096)

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PENNSYLVANIA ET AL.,
Defendants and Appellants.

Filed: January 29, 2001

OPINION

Appeals from a judgment and post-judgment orders of the Superior Court of California, County of Orange, Nancy Wieben Stock and Raymond J. Ikola, Judges. Motion to

Augment the record on appeal. Judgment and post-judgment orders affirmed. Motion granted.

Albert Weiland & Golden and Marcus M. Kaufman; Stephan, Oringher, Richman & Theodora and Robert M. Dato for Plaintiff and Appellant.

Horvitz & Levy, Mitchell C. Tilner and Peter Abrahams; Lewis, D'Amato, Brisbois & Bisgaard, R. Gaylord Smith and Michael W. Connally for Defendants and Appellants.

* * *

Plaintiff Textron Financial Corporation sued defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union) and others over a refusal to honor a claim for insurance benefits concerning property damage to a commercial bus in which it held a security interest. Plaintiff settled with two parties and proceeded to trial against National Union and American International Adjustment Company, Inc. (AIAC), National Union's claims adjuster. After a lengthy trial divided into three phases, the trial court entered judgment on a jury's special verdict awarding plaintiff $165,414.40 in compensatory damages and $10 million in punitive damages against National Union. The court entered judgment, including costs, for AIAC against plaintiff.

Both plaintiff and National Union filed post-judgment motions. The trial court denied National Union's motion for judgment notwithstanding the verdict and plaintiff's motion for new trial, but conditionally granted National Union a new trial unless plaintiff agreed to reduce the punitive damage award to $1.7 million. Plaintiff agreed to the remittitur. The court also struck plaintiff's request for expert witness fees.

National Union appeals from the judgment and the denial of its motion for judgment notwithstanding the verdict, challenging both the punitive damage award on several grounds, and the trial court's refusal to offset the amounts plaintiff received in the pre-trial settlements. Plaintiff

appeals, challenging the trial court's striking of its cause of action for unfair business practices, the judgment in favor of AIAC, including costs, the remittitur of punitive damages, and the denial of its request for expert witness fees.

FACTS

Il Sung Ko operated a tour bus company, Taeguk Tour and Sightseeing (Taeguk). Plaintiff loaned Ko funds to purchase a bus, receiving in return a security interest in the vehicle. The security agreement required Ko to insure the bus. Ko obtained a National Union liability insurance policy through D. W. Ferguson & Associates, Inc. (Ferguson), an independent insurance brokerage. The policy was issued through TRM International, Inc. (TRM), a company appointed by National Union to solicit, bind, write, and administer policies for its commercial bus program. The policy listed plaintiff as a loss payee and required National Union to mail plaintiff notice in advance if it cancelled the policy.

Taeguk suffered a downturn in business and Ko failed to timely pay his insurance premiums. In October 1992, TRM sent Ko notice it intended to cancel the policy. TRM did not send a copy of the cancellation notice to plaintiff. The policy terminated November 27.

Beginning in late October and throughout November, Ferguson and Taeguk discussed reducing the insurance premiums by deleting coverage for some of Ko's vehicles. Ferguson also corresponded with a TRM underwriter about the situation, proposing the issuance of a new policy covering only some of Ko's busses. The underwriter suggested an alternative whereby TRM would reinstate the original policy and give Ko a credit against his policy's premium if he agreed to certain conditions, which included delivering the license plates of two buses to Ferguson and temporarily suspending use of those vehicles. Plaintiff presented expert testimony that, unlike a transaction where a vehicle is deleted from a policy, the alternative approach implemented a

procedure described as lay-up credit. Under a lay-up credit, the insured maintains coverage on a vehicle while it is not being operated.

Ko agreed to this proposal, and on December 1, TRM reinstated the policy effective as of November 27. The bus encumbered by plaintiff's security interest was one of the vehicles Ko intended not to use. Plaintiff did not receive notice of the policy reinstatement with the endorsement which reflected Ko's business received a premium credit due to the vehicle's non-use. National Union claimed it sent a copy of this endorsement to plaintiff, but plaintiff denied receiving it.

In January 1993, the bus encumbered by plaintiff's lien suffered extensive damage when it collided with another vehicle on a public highway. At Taeguk's request, Ferguson submitted a notice of claim to AIAC. On February 4, TRM sent AIAC a notice verifying coverage for the vehicle and confirming plaintiff as a loss payee. However, after further correspondence with Taeguk and TRM, AIAC denied the claim, asserting the bus had been deleted from the policy before the accident. TRM prepared an endorsement deleting the bus from the policy (Number 8) on February 16. This endorsement purported to be effective as of December 1, 1992.

In late 1993, Ko defaulted on plaintiff's loan. Plaintiff then learned about the accident and contacted Ferguson concerning insurance benefits to repair the vehicle. Ferguson informed plaintiff the bus had been removed from the policy before the accident. Plaintiff sued Ko, recovering a judgment against him and incurring $3,859.50 in legal fees in the process. However, Ko filed bankruptcy and discharged the debt.

Plaintiff submitted a claim to National Union for benefits under the insurance policy. At that time, it possessed only a certificate of insurance, not a copy of the policy.

AIAC also handled plaintiff's claim. TRM informed AIAC the encumbered bus had been deleted from the policy before the accident and sent it a copy of endorsement number 8. A certificate of mailing on that copy covered the part of the endorsement reflecting the date TRM had prepared it. After an AIAC claims manager discussed the matter with John Lavin, a senior underwriter with the division handling National Union's bus program, and Tom Spangenberg, TRM's president, AIAC advised plaintiff the claim was being denied. The basis of the denial was that Ko deleted the bus from the policy before the accident, and TRM and AIAC concluded National Union's policy did not obligate it to give plaintiff advance notice of the deletion. National Union did not send plaintiff a copy of the policy until August 1994. Again, the portion of endorsement Number 8 displaying the date on which it had been prepared was covered by the mailing certificate.

PROCEDURAL BACKGROUND

The trial's first phase dealt with plaintiff's breach of contract claim against National Union. The court found, as a matter of law, the insurance contract's loss-payable clause constituted a separate agreement between plaintiff and National Union, obligating National Union to provide 30 days' notice of the policy's cancellation or the bus's deletion from it, and that National Union failed to comply with this requirement. The jury subsequently returned a special verdict awarding plaintiff $61,513.80 under the policy.

The second phase involved plaintiff's causes of action for bad faith against National Union and fraud against both National Union and AIAC. The jury returned a special verdict finding National Union violated the policy's implied covenant of good faith and fair dealing and that it acted with oppression, malice, and fraud in doing so. The jury also returned a special verdict, finding National Union liable for intentional misrepresentation and concealment, and awarded plaintiff $3,859.80 in damages. Based on its interpretation

of the jury's answers in the special verdict, the trial court entered judgment for AIAC on the fraud count.

During this phase, the trial court also ruled plaintiff could recover $30,268.16 in attorney fees as damages under *Brandt* v. *Superior Court* (1985) 37 Cal.3d 813. The parties stipulated plaintiff was entitled to $55,616.34 in costs pursuant to *Brandt*. Subsequently, the court denied National Union's request to offset the pretrial settlements plaintiff received from Ferguson ($26,500) and TRM ($62,500) against the compensatory award imposed on it.

The trial's third phase dealt with punitive damages. The jury returned a special verdict assessing $10 million in punitive damages against National Union which the trial court subsequently reduced to $1.7 million. In addition, the judgment awarded plaintiff compensatory damages, consisting of the policy benefits plus interest, the legal expenses recoverable under *Brandt* v. *Superior Court*, supra, 37 Cal.3d 813, and the damages for fraud. Finally, the court awarded AIAC $10,277.52 in costs against plaintiff.

DISCUSSION

PLAINTIFF'S APPEAL

Demurrer to the Unfair Business Practices Cause of Action

The complaint's fourth count sought injunctive and restitutionary relief under Business and Professions Code section 17200 et seq. against National Union and AIAC for "engag[ing] in unfair competition" in "handling [of plaintiff's] claim, and the claims of other persons." Plaintiff alleged National Union, "aided and abetted" by AIAC, "used misleading documents to falsely suggest that it would provide insurance . . . where it had no intention to do so," and "falsely suggested that it would . . . provid[e] timely notice of [policy] cancellations," "misrepresented the terms and meaning of its policies . . . to provide a pretext for its refusal to provide timely notice," and "engaged in a pattern and

practice of wrongful and false cancellations of insurance policies . . . ."

Relying on *Moradi-Shalal* v. *Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, National Union and AIAC generally demurred to this count. The trial court sustained the demurrers without leave to amend. Citing *State Farm Fire & Casualty Co.* v. *Superior Court* (1996) 45 Cal.App.4th 1093, plaintiff contends the trial court's ruling was erroneous.

Moradi-Shalal held the Unfair Insurance Practices Act (Ins. Code, § 790 et seq.; UIPA) does not create a private cause of action against insurers who violate its provisions. (*Moradi-Shalal* v. *Fireman's Fund Ins. Companies*, *supra*, 46 Cal.3d at pp. 304-305.) This rule applies to both first party and third party claims. (*Maler* v. *Superior Court* (1990) 220 Cal.App.3d 1592, 1597-1598; *Zephyr Park* v. *Superior Court* (1989) 213 Cal.App.3d 833, 836-838.) While insurance companies are subject to California laws generally applicable to other businesses, including laws governing unfair business practices (Ins. Code, § 1861.03, subd. (a)), parties cannot plead around *Moradi-Shalal's* holding by merely relabeling their cause of action as one for unfair competition. (*Manufacturers Life Ins. Co.* v. *Superior Court* (1995) 10 Cal.4th 257, 283-284; *Maler* v. *Superior Court*, *supra*, 220 Cal.App.3d at p. 1598; *Safeco Ins. Co.* v. *Superior Court* (1990) 216 Cal.App.3d 1491, 1494.)

The specific allegations of wrongful conduct contained in plaintiff's fourth cause of action, using misleading documents and misrepresenting both the terms of the insurance policies and its obligations under them for its own benefit, are the type of activities covered by the UIPA. (Ins. Code, § 790.03, subds. (a) & (h).) In *Safeco Ins. Co.* v. *Superior Court*, *supra*, 216 Cal.App.3d 1491, the court ordered dismissal of an action which included a request for injunctive relief under Business and Professions Code section 17200 et seq. based on an insurer's allegedly unfair claims settlement practices. (*Id.* at pp. 1493-1494.) "Though the

issue is one of first impression, we have no difficulty in deciding the Business and Professions Code provides no toehold for scaling the barrier of *Moradi-Shalal*. . . . To permit plaintiff to maintain this action would render *Moradi-Shalal* meaningless." (*Id.* at p. 1494.) Under the foregoing cases, merely alleging these purported acts constitute unfair business practices under the unfair competition law is insufficient to overcome *Moradi-Shalal*.

In a few cases, the Supreme Court has allowed an action against an insurance company under the unfair competition law where the alleged conduct constituted an unlawful restraint on trade under the Cartwright Act (Bus. & Prof. Code, § 16700 et seq.), even though it also violated the UIPA. (*Quelimane Co.* v. *Stewart Title Guarantee Co.* (1998) 19 Cal.4th 26, 43-44; *Manufacturers Life Ins. Co.* v. *Superior Court*, *supra*, 10 Cal.4th at pp. 283-284.) "This conclusion does not compromise the rule of *Moradi-Shalal* in any way. The court concluded there that the Legislature did not intend to create new causes of action when it described unlawful insurance business practices in section 790.03, and therefore that section did not create a private cause of action under the UIPA. The court did not hold that by identifying practices that are unlawful in the insurance industry, practices that violate the Cartwright Act, the Legislature intended to bar Cartwright Act causes of action based on those practices." (*Manufacturers Life Ins. Co.* v. *Superior Court*, *supra*, 10 Cal.4th at p. 284.)

The case on which plaintiff relies, *State Farm Fire & Casualty Co.* v. *Superior Court*, *supra*, 45 Cal.App.4th 1093, held the plaintiff-insureds had sufficiently alleged a cause of action against their insurer under the unfair competition law based on allegations of conduct constituting common law fraud and breach of the implied covenant of good faith and fair dealing, even though the same conduct violated the UIPA. "While *Moradi-Shalal* clearly held that the Legislature did not intend to create new causes of action when it enacted section 790.03, it is also clear that the Legislature did not intend in any way to circumscribe the

previously existing common law right of an insured to seek redress for an insurer's fraudulent deception or breach of the covenant of good faith implied in the policy. . . . Thus, . . . common law claims remain as a firm legal basis on which an insured may rely to seek redress against an insurer." (*Id.* at pp. 1107-1108.)

The persuasiveness of *State Farm* has been undercut by the Supreme Court's subsequent disapproval of its definition of "unfair" business practices. Quoting from *People* v. *Casa Blanca Convalescent Homes, Inc.* (1984) 159 Cal.App.3d 509, *State Farm* declared: "The test of whether a business practice is unfair 'involves an examination of [that practice's] impact on its alleged victim, balanced against the reasons, justifications and motives of the alleged wrongdoer. In brief, the court must weigh the utility of the defendant's conduct against the gravity of the harm to the alleged victim . . . . [Citations.]' . . . . [A]n 'unfair' business practice occurs when that practice 'offends an established public policy or when the practice is immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers.' [Citation.]" (*State Farm Fire & Casualty Co.* v. *Superior Court, supra*, 45 Cal.App.4th at pp. 1103-1104, fn. omitted.)

In *Cel-Tech Communications, Inc.* v. *Los Angeles Cellular Telephone Co.* (1999) 20 Cal.4th 163, the Supreme Court found this definition "too amorphous and provid[ing] too little guidance to courts and businesses." (*Id.* at pp. 184-185.) While *Cel-Tech Communications* limited its discussion to the context of an action between competitors, the court concluded, "any finding of unfairness to competitors under section 17200 be tethered to some legislatively declared policy or proof of some actual or threatened impact on competition," and that under Business and Professions Code section 17200, "the word 'unfair' . . . means conduct that threatens an incipient violation of an antitrust law, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law . . . ." (*Id.* at pp. 186-187, fn. omitted. See *Schnall* v. *Hertz Corp.* (2000) 78 Cal.App.4th 1144,1165-1167 [applying *Cel-Tech*

Communications, Inc.'s standard in vehicle lessee's action against rental agency for allegedly concealing or obscuring the rental agreement's fuel service charge].)

Harmonizing *Moradi-Shalal*'s holding with the foregoing decisions supports a conclusion the trial court properly sustained the demurrers to plaintiff's unfair competition claim. First, the holding in *Safeco Ins. Co.* v. *Superior Court*, *supra*, 216 Cal.App.3d 1491 supports this result. Second, this case is distinguishable from *Quelimane* and *Manufacturers Life* in two respects. Neither decision involved an action by an insured or a third party based on the insurer's alleged failure to comply with a policy or to provide benefits. In *Quelimane*, parties who acquired real estate at tax sales sued title insurance companies for refusing to issue policies on their property. *Manufacturers Life* concerned an insurance agency's action against insurance companies for boycotting the agency. Also, in both cases the plaintiff alleged a Cartwright Act violation as the basis for its unfair competition cause of action. Finally, given the Supreme Court's disapproval of *State Farm*'s "amorphous" definition of "unfair" practices and its focus on legislatively declared public policy, reliance on general common law principles to support a cause of action for unfair competition is unavailing.

Under these circumstances, the trial court properly found plaintiff failed to state a cause of action against National Union and AIAC for unfair business practices.

The Jury's Phase Two Findings

During the second phase, the jury returned a special verdict containing findings on the elements of two theories of deceit, intentional misrepresentation and concealment of a material fact. The jury's responses reflect it found both National Union and AIAC made representations of a material fact on which plaintiff justifiably relied to its injury, and that both defendants made the representations "recklessly without knowing whether [they were] true or false." However, the jury concluded AIAC did not know the representations were

false, and did not make them with the intent to defraud plaintiff. On the concealment theory, the jury found both defendants concealed or suppressed a material fact which resulted in injury to plaintiff, but also found AIAC did not intentionally conceal or suppress a material fact with the intent to defraud plaintiff. In addition, the jury concluded both defendants were "guilty of fraud, malice, or oppression in the conduct upon which [it] based [its] finding of liability . . . ."

When the jury returned its special verdict, the court discussed the inconsistency in the findings with counsel, and ultimately ruled AIAC "is not liable for fraud or concealment." Plaintiff argues the trial court erred by construing the jury's findings to exonerate AIAC.

The distinction between a general verdict and a special verdict is that under the former a jury "pronounce[s] generally upon all or any of the issues," while the latter is one "by which the jury find the facts only, leaving the judgment to the court." (Code Civ. Proc., § 624.) In a case "[w]here a special finding of facts is inconsistent with the general verdict, the former controls the latter, and the court must give judgment accordingly." (Code Civ. Proc., § 625; see also *Tavaglione* v. *Billings* (1993) 4 Cal.4th 1150, 1156-1157; *Bond* v. *DeWitt* (1954) 126 Cal.App.2d 540, 544.)

The jury's findings that AIAC made representations recklessly but without knowing the statements were false are inherently inconsistent. A representation made recklessly without knowledge of its falsity is sufficient to establish scienter. (5 Witkin, Summary of Cal. Law (9th ed. 1988) Torts, § 705, p. 806.) However, on both fraud theories the jury found AIAC did not act with an intent to defraud plaintiff. An intent to induce a particular act by the plaintiff is essential to establish liability for either an intentional misrepresentation or concealment of a material fact. (*Conrad* v. *Bank of America* (1996) 45 Cal.App.4th 133, 157; 5 Witkin, Summary of Cal. Law, *supra*, §§ 706 & 710, pp. 807, 810.) The absence of this element defeats plaintiff's

fraud claim against AIAC. Furthermore, the finding relevant to defendants' punitive damages liability was in the nature of a general verdict and is subordinate to the jury's specific finding of no intent to defraud. Thus, the trial court properly entered judgment for AIAC on the fraud claim.

Plaintiff contends AIAC could be found liable either as a co-conspirator of National Union or on a theory of negligent misrepresentation. These contentions are without merit.

First, since plaintiff did not assert the latter theory at trial, and the court did not instruct the jury on it, it is now too late to do so. (*Overgaard* v. *Johnson* (1977) 68 Cal.App.3d 821, 826.) Second, while the court did instruct the jury on conspiracy as a basis for imposing liability, as plaintiff concedes, the jury was not asked to return a special verdict on this allegation. Had the jury concluded AIAC was liable as a co-conspirator with National Union, it should have returned a finding of an intent to defraud.

A review of plaintiff's closing argument also reflects it relied on the representations and conduct of AIAC's employees, not conspiracy, to support its fraud claim. In fact, while discussing the question of whether National Union acted with malice, plaintiff's counsel suggested no conspiracy existed. "An insurance company whose job is to . . . investigate the situation thoroughly, concealing information which it knows is going to lead to a discovery that there's coverage – even concealing that information from its own claims people so that they won't have a guilty conscience about denying the claim – that's malice."

The trial court properly entered judgment for AIAC on the fraud claim.

The Attorney Fees Damage Award

Plaintiff retained legal counsel under an agreement requiring it to pay counsel 40 percent of all amounts recovered in the case. After a lengthy discussion, the trial court limited the attorney fees plaintiff could recover as

damages under *Brandt* v. *Superior Court*, *supra*, 37 Cal.3d 813, to 40 percent of the amount recovered as policy benefits during the trial's first phase. Plaintiff attacks this ruling and claims it should have been allowed to recover the reasonable value of counsel's services which it calculates is nearly $300,000 greater than the amount awarded by trial court. This contention lacks merit.

Brandt held attorney fees reasonably incurred to compel payment of policy benefits tortiously withheld by an insurer are recoverable as an element of damages. (*Brandt* v. *Superior Court*, *supra*, 37 Cal.3d at pp. 815, 817.) "When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense. The attorney's fees are an economic loss – damages – proximately caused by the tort. [Citation.]" (*Id.* at p. 817.)

The retainer agreement required plaintiff to pay counsel 40 percent of all sums recovered in this action. It had no further legal obligation to pay counsel for the legal services rendered to it. *Brandt* expressly held the "fees recoverable . . . may not exceed the amount attributable to the attorney's efforts to obtain the rejected payment due on the insurance contract." (*Brandt* v. *Superior Court*, *supra*, 37 Cal.3d at p. 819.) Plaintiff cites no authority permitting a post-trial modification of the retainer agreement. Thus, the trial court did not err by limiting the attorney fee damage award to the percentage specified in the parties' contingency agreement.

The Post-Judgment Costs Award

Plaintiff attacks the trial court's post-judgment rulings concerning the award of costs on two grounds. Both arguments lack merit.

First, it disputes the court's finding AIAC was a prevailing party. Plaintiff argues that since National Union and AIAC filed a joint answer to the complaint and were represented by

the same counsel during trial, they held a unity of interest which precludes AIAC from acquiring this status.

Code of Civil Procedure section 1032 defines prevailing party to include "a defendant in whose favor a dismissal is entered, a defendant where neither plaintiff nor defendant obtains any relief, and a defendant as against those plaintiffs who do not recover any relief against that defendant. . . . [I]n situations other than as specified, the 'prevailing party' shall be as determined by the court, and under those circumstances, the court, in its discretion, may allow costs or not and, if allowed may apportion costs between the parties on the same or adverse sides . . . ." (Code Civ. Proc., § 1032, subd. (a)(4).) In conformity with this statute, the case law holds that where only one of multiple, jointly-represented defendants presenting a unified defense prevails in an action, the trial court has discretion to award or deny costs to that party. (*Webber* v. *Inland Empire Investments, Inc.* (1999) 74 Cal.App.4th 884, 920; *Slavin* v. *Fink* (1994) 25 Cal.App.4th 722, 725-726; *Smith* v. *Circle P Ranch Co.* (1978) 87 Cal.App.3d 267, 272.)

Plaintiff asserts the trial court did not exercise its discretion in this case, citing a statement by the trial judge during the hearing on the motion to strike AIAC's cost bill. However, the court made that comment in response to plaintiff's contention "no evidence" exists "to support any particular allocation" between AIAC and National Union, and that the latter entity presumably "fronted" AIAC's trial expenses. The record as a whole does not support a conclusion the trial court failed to exercise its discretion concerning AIAC's status and its recovery of costs.

The related arguments also fail. Contrary to plaintiff's assertion this is not a case where it established wrongdoing against AIAC, but simply failed to recover a monetary award. The jury found AIAC did not commit fraud. Furthermore, since the injunctive relief claim had been previously dismissed, this was an action for damages. Thus, the evidence indicating AIAC subsequently modified its

operating procedures concerning claims handling does not preclude it from being deemed a prevailing party.

Second, plaintiff contends the trial court erred by denying its recovery of expert witness fees under Code of Civil Procedure section 998. Nearly a year before trial, plaintiff served on National Union and AIAC an unsuccessful pretrial offer to compromise proposing "to allow judgment be taken . . . against defendants" for $626,489.26. In denying plaintiff's request for expert witness fees, the court cited *Taing* v. *Johnson Scaffolding Co.* (1992) 9 Cal.App.4th 579.

Code of Civil Procedure section 998, subdivision (d) authorizes the court to award a prevailing plaintiff its expert witness fees if the plaintiff made timely pretrial offer to compromise which the defendant does not accept, and "the defendant fails to obtain a more favorable judgment . . . ." In *Taing*, the court reversed an award of costs, declaring "if a plaintiff elects to submit a section 998 offer in cases involving multiple defendants, the offer to any defendant against whom the plaintiff seeks to extract penalties for nonacceptance must be sufficiently specific to permit that individual defendant to determine the exact amount plaintiff is seeking from him or her." (*Taing* v. *Johnson Scaffolding Co.*, *supra*, 9 Cal.App.4th at p. 586.) *Taing* explained its rule as follows: "[A]n unapportioned offer by a single plaintiff to multiple defendants . . . requires any defendant who wants to accept to obtain the concurrence of his or her codefendants. This places a reasonable defendant at the mercy of codefendants whose refusal to settle may be unreasonable." (*Id.* at p. 585.)

National Union and AIAC were not jointly and severally liable to plaintiff. (Cf. *Steinfeld* v. *Foote-Goldman Proctologic Medical Group, Inc.* (1996) 50 Cal.App.4th 1542, 1547-1549.) The complaint sought recovery against National Union on theories of breach of contract, bad faith, and fraud. AIAC was alleged to be liable only on the latter theory. Furthermore, the evidence relating to each defendant's liability for fraud was separate. Thus, the trial

court did not err by exercising its discretion to deny recovery of expert witness fees in this case.

NATIONAL UNION'S APPEAL

Denial of an Offset

National Union moved to have the settlement amounts plaintiff received from Ferguson and TRM offset against the damages plaintiff recovered from it. The trial court issued a lengthy written order denying the request as to both the contractual damages and the tort damages recovered by plaintiff. National Union contends the trial court erred by denying an offset in this case.

Consistent with the general rule imposing on a party the burden of proving the existence or nonexistence of each fact essential to a claim or defense (Evid. Code, § 500), "[a] defendant seeking an offset against a money judgment has the burden of proving the offset. [Citation.]" (*Conrad* v. *Ball Corp.* (1994) 24 Cal.App.4th 439, 444.)

With respect to plaintiff's contractual recovery, an insured is entitled to receive compensation in accordance with the policy terms, and an insurer cannot reduce the amount recoverable "merely because [the insured] has 'collateral contracts or relations with third persons which relieve him wholly or partly from the loss against which the insurance company agreed to indemnify him.' [Citations.]" (*Strickland* v. *Federal Ins. Co.* (1988) 200 Cal.App.3d 792, 801, quoting *Hughes* v. *Potomac Ins. Co.* (1962) 199 Cal.App.2d 239, 251, disapproved on another point in *Sabella* v. *Wisler* (1963) 59 Cal.2d 21, 34.) An insurer's right to recoup payment of policy benefits is covered by the principle of subrogation. To qualify for subrogation, the insurer must pay the insured's loss. (*Sapiano* v. *Williamsburg Nat. Ins. Co.* (1994) 28 Cal.App.4th 533, 538; *Chase* v. *National Indemnity Co.* (1954) 129 Cal.App.2d 853, 861-862.)

National Union refused to pay any policy benefits to plaintiff. The cases on which it relies to establish an offset

against the contract damages involve an insured's recovery of tort damages and whether the collateral source rule applied. Its contention the trial court "misread" *Kardly* v. *State Farm Mut. Auto. Ins. Co.* (1989) 207 Cal.App.3d 479 is incorrect. Contrary to National Union's claim, *Kardly* did not hold the insurer waives the right of subrogation by breaching the insurance contract. The part of the *Kardly* opinion National Union quotes refers to the facts of another appellate decision. (*Id.* at p. 489.) Thus, the trial court properly refused to offset the Ferguson and TRM settlements against the contractual damage award.

As for plaintiff's recovery of tort damages, the trial court agreed the collateral source doctrine did not apply because Ferguson and TRM could not be deemed collateral sources under the facts of this case. However, the court detailed the potential liability facing Ferguson and TRM, and found their potential liability exceeded $261,000 which included nonduplicative exposure exceeding $96,000. Applying the tort of another doctrine, the court concluded the settlement sums paid by Ferguson and TRM should not be offset against plaintiff's recovery from National Union.

Generally, a party cannot obtain double recovery for the same wrong where joint or concurrent tortfeasors are jointly and severally liable for the same wrong. (6 Witkin, Summary of Cal. Law, *supra*, Torts, § 1322, at p. 779.) "[I]t has long been recognized that if one tortfeasor pays partial compensation to the plaintiff, the liability of other tortfeasors will be correspondingly reduced: '. . . payments by one tortfeasor on account of a harm for which he and another are each liable, diminish the amount of the claim against the other whether or not it was so agreed at the time of payment and whether the payment was made before or after judgment. Since the plaintiff can have but one satisfaction, evidence of such payments is admissible for the purpose of reducing pro tanto the amount of the damages he may be entitled to recover.' [Citations.]" (*Krusi* v. *Bear, Stearns & Co.* (1983) 144 Cal.App.3d 664, 673.)

Where tortious acts by separate persons produce the same indivisible injury, each person is liable for the whole loss even if they did not act in concert. (*Sanchez* v. *Bay General Hospital* (1981) 116 Cal.App.3d 776, 796.) Thus, while plaintiff sued National Union for breach of contract, breach of the implied covenant of good faith and fair dealing, and fraud, but only sought damages against Ferguson and TRM for negligence, the injury it suffered was the same.

However, the court did find the tort of another doctrine applicable to this case. "A person who through the tort of another has been required to act in the protection of his interests by bringing or defending an action against a third person is entitled to recover compensation for the reasonably necessary loss of time, attorney's fees, and other expenditures thereby suffered or incurred. [Citations.]" (*Prentice* v. *North Amer. Title Guar. Corp.* (1963) 59 Cal.2d 618, 620.)

Generally, a party seeking to recover litigation costs under this rule must plead and prove the claim. (*Hsu* v. *Abbara* (1995) 9 Cal.4th 863, 869, fn. 4.) While plaintiff did not do so here, the potential for its recovery of damages from Ferguson and TRM was made known to them during pretrial discovery. Furthermore, had it not settled with Ferguson and TRM, plaintiff could have amended the complaint to assert its right to recover the fees and expenses incurred in its action against National Union.

The record reflects National Union failed to establish the trial court erred by denying its request for an offset.

PUNITIVE DAMAGES

Introduction

Both parties attack the punitive damage award. National Union challenges the sufficiency of the evidence supporting the recovery of exemplary damages, the court's refusal to instruct the jury National Union could only be subject to punitive damages based on its own employees' conduct, and

the constitutionality of the award imposed on it. Plaintiff contends the trial court erred by reducing the punitive damage award to $1.7 million.

Sufficiency of the Evidence

National Union claims its own conduct was not oppressive, fraudulent, or malicious, TRM's activity cannot be attributed to it, and it did not ratify TRM's actions.

Civil Code section 3294 authorizes the award of punitive damages in any "action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice . . . ." (Civ. Code, § 3294, subd. (a).) In *Egan* v. *Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d 809, the Supreme Court upheld an award of punitive damages against an insurer based on evidence two employees, a claims manager and a claims adjuster, failed to adequately investigate the insured's claims under a disability insurance policy. "The determination whether employees act in a managerial capacity, however, does not necessarily hinge on their 'level' in the corporate hierarchy. Rather, the critical inquiry is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy. When employees dispose of insureds' claims with little if any supervision, they possess sufficient discretion for the law to impute their actions concerning those claims to the corporation." (*Id.* at pp. 822-823.)

Subsequently, the Legislature amended Civil Code section 3294 to provide, "[a]n employer shall not be liable for [punitive] damages . . . based upon acts of an employee of the employer, unless the employer had advance knowledge of the unfitness of the employee and employed him or her with a conscious disregard of the rights or safety of others or authorized or ratified the wrongful conduct for which the damages are awarded or was personally guilty of oppression, fraud, or malice. With respect to a corporate employer, the advance knowledge and conscious disregard, authorization,

ratification or act of oppression, fraud, or malice must be on the part of an officer, director, or managing agent of the corporation." (Civ. Code, § 3294, subd. (b).)

In *White* v. *Ultramar, Inc.* (1999) 21 Cal.4th 563, the Supreme Court considered the effect of this amendment in an action for wrongful termination. The plaintiff, a convenience store employee, had been fired by a manager who was responsible for eight stores, covering sixty-five employees. The jury awarded plaintiff both compensatory and punitive damages.

In affirming, the Supreme Court concluded that "in amending section 3294, the Legislature intended (like *Egan*, *supra*, 24 Cal.3d at p. 823) to limit corporate punitive damage liability to those employees who exercise substantial independent authority and judgment over decisions that ultimately determine corporate policy." (*White* v. *Ultramar, Inc.*, *supra*, 21 Cal.4th at p. 573.) The court noted "section 3294, subdivision (b), placed ['managing agent'] next to the terms 'officer' and 'director,' intending that a managing agent be more than a mere supervisory employee. The managing agent must be someone who exercises substantial discretionary authority over decisions that ultimately determine corporate policy. Thus, by selecting the term 'managing agent,' and placing it in the same category as 'officer' and 'director,' the Legislature intended to limit the class of employees whose exercise of discretion could result in a corporate employer's liability for punitive damages." (*Ibid.*) The critical factor " ' ". . . is the degree of discretion the employees possess in making decisions that will ultimately determine corporate policy." [Citation.]' " (*Id.* at p. 573.)

The agency agreement between National Union and TRM and the evidence in this case shows TRM had broad discretion over National Union's bus insurance program. TRM could "solicit, bind, write and administer insurance" policies, and "exercise [its] independent judgment as to the time, place and manner of soliciting insurance and servicing

policyholders." There was evidence AIAC directed its employees to contact TRM when seeking coverage verification. In this case, TRM participated in issuing the policy to Ko, in subsequently canceling it, and then reinstating a modified version of it. Later, when Ko submitted a claim on the bus, TRM initially issued a coverage determination, but then prepared an endorsement deleting the vehicle from the policy, and advised AIAC to deny the claim. Furthermore, TRM's president was in contact with both AIAC and the senior management of the division handling National Union's bus program when plaintiff's claim was being considered, and participated in the ultimate decision to deny it. This evidence supports the jury's conclusion TRM was National Union's managing agent, thereby subjecting it to punitive damages under Civil Code section 3294. (*White* v. *Ultramar, Inc.*, *supra*, 21 Cal.4th at p. 577; *Egan* v. *Mutual of Omaha Ins. Co.* (1979) 24 Cal.3d at p. 823.)

In light of this conclusion it is unnecessary to consider National Union's additional claims concerning instructional error and the insufficiency of the evidence based on its own conduct.

Validity of the Trial Court's Remittitur

The trial court issued a post-judgment order conditionally granting National Union a new trial on the insurance bad faith and fraud counts, and plaintiff's right to receive punitive damages unless the latter agreed to reduce the punitive damage award to $1.7 million. Plaintiff timely consented to the remittitur. After National Union filed its appeal, plaintiff cross-appealed and now challenges the remittitur's validity.

A trial court has the discretion to conditionally grant a new trial unless the plaintiff consents to a reduction of a damages award where the court independently determines the jury's award is excessive. (Code Civ. Proc., § 662.5, subd. (b); *Schelbauer* v. *Butler Manufacturing Co.* (1984) 35 Cal.3d 442, 452-453; *West* v. *Johnson & Johnson Products, Inc.*

(1985) 174 Cal.App.3d 831, 876.) Reversal of the ruling is allowed only where there is no substantial basis in the record to support the reasons articulated by the trial court for its decision. (Code Civ. Proc., § 657; *Jahn* v. *Brickey* (1985) 168 Cal.App.3d 399, 408.)

The court noted the ratio of the original punitive damage award to compensatory damages (60 to 1) created a presumption the jury's verdict was the result of passion and prejudice. (*Rosener* v. *Sears, Roebuck & Co.* (1980) 110 Cal.App.3d 740, 752.) Plaintiff focuses much its argument on the reprehensible nature of National Union's conduct. While the court agreed the evidence supported the jury's conclusion National Union had acted reprehensibly, it concluded the jury had placed too much emphasis on National Union's financial wealth and failed to adequately consider the relationship between the injury suffered by plaintiff and the amount of the punitive damage award. The court noted this lawsuit involves an action by one corporate entity against another corporate entity to recover only for economic loss, the value of plaintiff's security interest in a damaged bus. Given these circumstances, the trial court noted upholding the original award raised serious constitutional concerns.

Plaintiff also challenges the portion of the remittitur order requiring it to choose between a reduction in punitive damages and a new trial on *both* liability and the amount of punitive damages. In so ruling, the trial court cited *Medo* v. *Superior Court* (1988) 205 Cal.App.3d 64. Plaintiff relies on *Torres* v. *Automobile Club of So. California* (1997) 15 Cal.4th 771 in challenging the trial court's ruling.

Torres held Civil Code section 3295, subdivision (d) did not require an *appellate* court which reverses an excessive punitive damage award to order a new trial on all issues, including liability and the amount of compensatory damages. (*Id.* at pp. 777-781.) In so ruling, *Torres* distinguished *Medo*. (*Id.* at p. 780.) In *Medo*, the *trial* court ordered a new trial on all issues when the jury was discharged after

completion of the liability phase. While agreeing with the plaintiffs' assertion that the defendants had waived their right to have the same jury determine both liability and the right to punitive damages, the appellate court nonetheless noted, "[p]unitive damages are not simply recoverable in the abstract. They must be tied to oppression, fraud or malice *in the conduct which gave rise to liability in the case.* Thus . . ., the instruction on punitive damages[] tells the jury that in arriving at an award of punitive damages, it is to consider the reprehensibility of the conduct of the defendant and that the punitive damages must bear a reasonable relation to the actual damages. In order for a jury to evaluate the oppression, fraud or malice in the conduct giving rise to liability in the case, it must consider the conduct giving rise to liability." (*Medo* v. *Superior Court*, *supra*, 205 Cal.App.3d at p. 68.)

However, even assuming the trial court erred by relying on *Medo* to order a new trial on all issues if plaintiff refused to accept a reduction in the punitive damage award, the ruling does not require reversal. As the trial judge concluded, the jury's $10 million punitive damage award was clearly constitutionally suspect. Thus, ordering a remittitur in this case was appropriate under the circumstances.

Constitutionality of the Award

Finally, National Union contends that even the $1.7 million punitive damage award is excessive and unconstitutional. This argument lacks merit.

Punitive damages have two purposes; punish the wrongdoer and deter similar misconduct in the future by making an example of the wrongdoer. (*PPG Industries, Inc.* v. *Transamerica Ins. Co.* (1999) 20 Cal.4th 310, 317; *Stevens* v. *Owens-Corning Fiberglas Corp.* (1996) 49 Cal.App.4th 1645, 1658.) "The essential question for the jury, the trial court, and the appellate courts is whether the amount of the award substantially serves the public interest in punishment and deterrence. The California Supreme

Court has established three criteria for making that determination: (1) the reprehensibility of the defendant's misdeeds; (2) the amount of compensatory damages, though there is no fixed ratio for determining whether punitive damages are reasonable in relation to actual damages; and (3) the defendant's financial condition. [Citations.]" (*Stevens* v. *Owens-Corning Fiberglas Corp.*, *supra*, 49 Cal.App.4th at p. 1658.) On appeal, a judgment awarding punitive damages is presumed to be correct and will be reversed only if the record, viewed most favorably to the judgment, reflects the award is the result of passion or prejudice. (*Ibid.*)

The United Supreme Court has recognized that an excessive punitive damage award may also violate a person's constitutional right to due process of law. (*BMW of North America, Inc.* v. *Gore* (1996) 517 U.S. 559, 562; *TXO Production Corp.* v. *Alliance Resources Corp.* (1993) 509 U.S. 443, 454.) In *BMW*, the court noted: "Elementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive fair notice not only of the conduct that will subject him to punishment, but also of the severity of the penalty that a State may impose." (*BMW of North America, Inc.* v. *Gore*, *supra*, 509 U.S. at p. 574, fn. omitted.) The court identified "[t]hree guideposts" to consider in analyzing the constitutionality of a punitive damage award: "[T]he degree of reprehensibility [of the wrongdoer's conduct]; the disparity between the harm or potential harm suffered . . . and [the] punitive damages award; and the difference between this remedy and the civil penalties authorized or imposed in comparable cases." (*Id.* at pp. 574-575.)

The record reflects the present award is permissible under both state and federal law. While it is true the loss involved only economic injury, the evidence reflects National Union engaged in reprehensible conduct. To enforce the purposes of punishing the wrongdoer and deterring similar future wrongful conduct, the award necessarily had to be large to affect a corporate entity such as National Union. "The wealthier the wrongdoer, the larger the punitive damage

award must be to meet the goals of punishment and deterrence. [Citations.]" (*Stevens* v. *Owens-Corning Fiberglas Corp.*, *supra*, 49 Cal.App.4th at p. 1658.)

National Union does not dispute the fact reprehensible conduct occurred in this case. It only argues TRM, not it, committed the wrongdoing. But Civil Code section 3294, subdivision (b) permits the imposition of punitive damages on a person held vicariously liable for another's actions. National Union also focuses on the ratio between the punitive damage award and the compensatory damage award. While punitive damages must bear a reasonable relation to the actual damages suffered by the plaintiff, no fixed ratio exists to determine the proper proportion between them. (*Finney* v. *Lockhart* (1950) 35 Cal.2d 161, 164; *Zhadan* v. *Downtown L. A. Motors* (1976) 66 Cal.App.3d 481, 498.)

Thus, we conclude the award of $1.7 million in punitive damages in this case is not excessive, nor does it violate National Union's constitutional right to due process of law.

DISPOSITION

The judgment and post judgment orders are affirmed. The motion to augment the record on appeal is granted. Each party shall bear its own costs on appeal.

RYLAARSDAM, J.

WE CONCUR:

SILLS, P. J.

O'LEARY, J.

APPENDIX B

SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF ORANGE

Case No. 734096

TEXTRON FINANCIAL CORPORATION, A DELAWARE CORPORATION,

Plaintiff,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA; AND AMERICAN INTERNATIONAL ADJUSTMENT COMPANY, INC.,

Defendant.

Assigned for All Purposes to:
Judge Raymond J. Ikola
Dept. 8

Filed: May 29, 1996
Trial Date: February 26, 1996

JUDGMENT

This action came on regularly for trial by jury, beginning on February 26, 1996, in Department 8 of the above-entitled Court, Honorable Raymond J. Ikola, presiding. Plaintiff Textron Financial Corporation ("Textron") appeared by its attorneys, Steven H. Gentry and David B. Ezra of Berger, Kahn, Shafton, Moss, Figler, Simon & Gladstone, and defendants National Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union") and American International Adjustment Company ("AIAC") appeared by their attorneys, R. Gaylord Smith and Michael Connally of Lewis, D'Amato, Brisbois & Bisgaard.

During the trial, the Court ruled that there was coverage for Textron's claim, as a matter of law. The Court concluded that the actions of the first named insured, Il Sung Ko, could not have terminated Textron's protection under the applicable policy.

During the trial, the Court granted National Union's motion for nonsuit, but only to the extent that Textron's complaint included allegations of a conspiracy to commit insurance bad faith. In all other respects, National Union's motions for nonsuit, and its motions for directed verdicts, were denied.

A jury of twelve persons was duly impaneled and sworn; witnesses testified; and after being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase I:

"We, the jury, find and report to the court our special verdict in phase 1 of the trial in this matter as follows:

1. What is the amount of money payable to Textron under the policy? $61,513.80 .

2. Did Textron fail to mitigate its damages?

Yes _____ No __x__

3. If your answer to the previous question was yes, state the amount of damages caused by Textron's failure to mitigate: _____.

Dated: March 14, 1996 /s/
Foreperson
Jon A. Ribble"

Thereafter, the Court ruled that Textron's attorney fee damages could not exceed the law firm's contingent percentage (40%) of the amounts unreasonably withheld by National Union (together with interest).

Based on the Court's ruling, evidence of time incurred by Textron's attorneys in an effort to compel payment of policy benefits was not presented to the jury. Textron and National Union stipulated, based on the ruling of the Court, that Textron's attorney fee recovery would be 40% of $61,513.80 (plus interest from January 25, 1994), together with expenses in the amount of $55,616.34.

After being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase II:

"We, the jury in the above entitled case, find the following on the questions submitted to us:

1. Do you find by a preponderance of the evidence that Nation[al] Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union") violated the implied covenant of good faith and fair dealing owing to Textron?

Yes x No _____

If you answer "No" to Question No. 1, then go to Question No. 5. If you answer "Yes", then answer Questions Nos. 2, 3, and 4.

2. Do you find by clear and convincing evidence that National Union was guilty of oppression in the conduct upon

which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes __x__ No _____

3. Do you find by clear and convincing evidence that National Union was guilty of malice in the conduct upon which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes __x__ No _____

4. Do you find by clear and convincing evidence that National Union was guilty of fraud in the conduct upon which you based your finding of liability for breach of the implied covenant of good faith and fair dealing?

Yes __x__ No _____

5. Did either defendant make a representation as to a past or existing material fact?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer Question No. 5 "No" as to both defendants, go to Question No. 15. If you answer Question No. 5 "Yes" as to either defendant, then answer the next question.

6. Was the representation false?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer Question No. 6 "No" as to both defendants, got [sic] to Question No. 15. If you answer Question No. 6 "Yes" as to either defendant, then answer questions 7a and 7b.

7a. Did either defendant know that the representation was false when it was made?

National Union: Yes __x__ No _____

AIAC: Yes _____ No __x__

7b. Did either defendant make the representation recklessly without knowing whether it was true or false?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer both Questions 7a and 7b "No" as to both defendants, go to Question No. 15. If you answer Question No. 7A or 7b "Yes" as to either defendant, then answer the next question.

8. Did either defendants make the representation with an intent to defraud the plaintiff?

National Union: Yes __x__ No _____

AIAC: Yes _____ No __x__

If you answer Question No. 8 "No" as to both defendants, go to Question No. 15. If you answer Question No. 8 "Yes" as to either defendant, then answer the next question.

9. Was the plaintiff aware of the falsity of the representation?

Yes _____ No __x__

If you answer Question No. 9 "Yes", go to Question No. 15. If you answer Question No. 9 "No", then answer the next question.

10. Did the plaintiff act in reliance upon the truth of the representation?

Yes __x__ No _____

If you answer Question No. 10 "No", go to Question No. 15. If you answer Question No. 10 "Yes", then answer the next question.

11. Was the plaintiff justified in relying upon the representation?

Yes __x__ No _____

If you answer Question No. 11 "No", go to Question No. 15. If you answer Question No. 11 "Yes", then answer the next question.

12. Did either defendant's misrepresentation cause plaintiff damage?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer Question No. 12 "No" as to both defendants, go to Question No. 15. If you answer Question No. 12 "Yes" as to either defendant, then answer the next question.

13. What is the total amount of all damage suffered by the plaintiff and caused by the reliance upon the truth of the representation?

Answer: $3859.50

If you answer Question No. 13 "No Damage", then go to Question No. 15. If you filled in a dollar amount in answer to Question No. 13, then answer the next question.

14. Do you find by clear and convincing evidence that either defendant was guilty of fraud, malice, or oppression in the conduct upon which you based your finding of liability for fraud?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

15. Did either defendant conceal or suppress a material fact?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer Question No. 15 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 15 "Yes" as to either defendant, then answer the next question.

16. Did either defendant intentionally conceal or suppress the material fact with the intent to defraud the plaintiff?

National Union: Yes __x__ No _____

AIAC: Yes _____ No __x__

If you answer Question No. 16 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 16 "Yes" as to either defendant, then answer the next question.

17. Was the plaintiff aware of the material fact at the time plaintiff acted?

Yes _____ No __x__

If you answer Question No. 17 "Yes", then sign and return the verdict. If you answer Question No. 17 "No", then answer the next question.

18. Would the plaintiff had acted in the way it did if it had known of the concealed or suppressed material fact?

Yes _____ No __x__

If you answer Question No. 18 "Yes", then sign and return the verdict. If you answer Question No. 18 "No", then answer the next question.

19. Did either defendant's concealment or suppression of the material fact cause plaintiff damage?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

If you answer Question No. 19 "No" as to both defendants, then sign and return the verdict. If you answer Question No. 19 "Yes", as to either defendant, then answer the next question.

20. What is the total amount of all damage suffered by the plaintiff and caused by the concealment or suppression of the material fact?

Answer: $3859.50

If you answer Question No. 20 "No Damage", then sign and return the verdict. If you filled in a dollar amount in answer to Question No. 20, then answer the next question.

21. Do you find by clear and convincing evidence that either defendant was guilty of fraud, malice, or oppression in the conduct upon which you based your finding of liability for the intentional concealment or suppression of a material fact?

National Union: Yes __x__ No _____

AIAC: Yes __x__ No _____

Please sign and date this verdict form.

Dated: April 11, 1996

Jon A. Ribble
/s/
Foreperson"

Based upon this verdict, the Court determined that AIAC was entitled to judgment in its favor.

After being duly instructed by the Court, the jury deliberated and thereon duly returned the following special verdict in Phase III:

"We, the jury in the above entitled action, find the following special verdict on the questions submitted to us:

1. Shall punitive damages be assessed against defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania?

Yes __x__ No _____

If your answer is "yes," please answer the next question. If your answer is "no," have your foreperson sign and date this special verdict.

2. We assess punitive damages against National Union Fire Insurance Company of Pittsburgh, Pennsylvania, as follows:

$10,000,000.00.

Please sign and date this verdict form.

Dated: April 12, 1996

Jon A. Ribble
/s/
Foreperson"

NOW, THEREFORE, IT IS ADJUDGED, ORDERED, AND DECREED as follows:

Plaintiff Textron Financial Corporation shall have and recover judgment against defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania:

1. For general and compensatory damages, $165,414.40 (representing $61,513.80 in unpaid policy benefits, $14,156.60 in interest on unpaid benefits from January 24, 1994 to May 14, 1996, $85,884.50 pursuant to *Brandt* v. *Superior Court*, and $3,859.50 in additional damages on the fraud cause of action);

2. For punitive damages, ten million dollars ($10,000,000.00);

3. Plus costs and disbursements in the amount of $39,280.31* . *(Per Order of 7-29-96)

Defendant American International Adjustment Company shall have judgment against plaintiff Textron Financial Corporation and shall recover costs and disbursements in the amount of $10,277.52 . (Per M.O. of 10-3-96)

DATED: 5/29/96 By: /s/ Raymond J. Ikola
RAYMOND J. IKOLA,
Judge of the Superior Court

APPENDIX C

SUPERIOR COURT OF THE STATE OF CALIFORNIA
COUNTY OF ORANGE

Case No. 73 40 96

TEXTRON FINANCIAL CORPORATION, A DELAWARE CORPORATION,

Plaintiff,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, ET AL.,

Defendants.

Filed: July 29, 1996

RULING AND ORDER CONDITIONALLY GRANTING NATIONAL UNION'S MOTION FOR NEW TRIAL

The court, having read and considered the Motion for New Trial filed herein by defendant National Union Fire Insurance Company of Pittsburgh, Pennsylvania ("National Union"), together with the papers filed in opposition to the motion by plaintiff Textron Financial Corporation ("Textron") and the papers filed in reply to the opposition by National Union, and having heard and considered the arguments made by both

parties at the hearing on the motion on July 25, 1996, now rules as follows:

National Union's Motion for New Trial is granted as to the causes of action for fraud and for breach of the implied covenant of good faith and fair dealing and the award of punitive damages on the ground that the award of punitive damages is excessive. The new trial will be as to National Union only. Provided, however, that the order granting a new trial is denied if Textron consents to a reduction of the $10 million award of punitive damages in the amount of $8.3 million to a total award of punitive damages in the amount of $1.7 million ($1,700,000.00). The court, in its independent judgment, has determined from the evidence that a punitive damage award of $1.7 million is fair and reasonable.

The reasons the court has conditionally granted the motion for new trial on the ground of excessive damages are as follows.

The jury was instructed, in connection with making its determination of whether to award punitive damages, to consider: (i) the reprehensibility of the conduct of the defendant; (ii) the amount of punitive damages which will have a deterrent effect on the defendant in the light of defendant's financial condition; and (iii) that punitive damages must bear a reasonable relation to the injury, harm, or damage actually suffered by the plaintiff." BAJI 14.72.2. The court has concluded that the jury gave undue emphasis to the second factor, i.e., the amount of damages which will have a deterrent effect in light of the defendant's financial condition, and insufficient emphasis to the third factor, i.e., the relationship between the damage suffered and the amount of the award. The punitive damages awarded by the jury amounted to slightly more 60 times the total compensatory award. In *Rosener* v. *Sears, Roebuck & Co.*, 110 Cal.App.3d 740, 752 (1980), the court referred to an award in which the ratio of punitive to compensatory damages was approximately 63 to 1, with a difference in the awards of $9.85 million, as "grossly disproportionate," raising "a

presumption that it was the result of passion or prejudice." *Id.* at 752. In the case at bar the ratio of punitive to compensatory damages is 60 to 1, and the difference is $9.83 million. The same presumption of passion or prejudice is as apparent in this case as it was in *Rosener*. The amount awarded by the jury greatly exceeds that which is necessary to deter future conduct of the type shown by the evidence in this case.

Further, the court is obliged to examine the award in light of the federal due process "guideposts" outlined by the U.S. Supreme Court in *BMW of North America* v. *Gore*, 96 D.A.R. 5747 (May 20, 1996), a decision announced after the jury reached its verdict. The first guidepost, described by the *BMW* court as "perhaps the most important indicium of the reasonableness of a punitive damages award" is "the degree of reprehensibility of the defendant's conduct." This guidepost matches one of the factors given to the jury to consider in this case consistent with *Neal* v. *Farmers Ins. Exchange*, 21 Cal.3d 910, 928 (1978). Although the court finds that the jury had sufficient evidence to find that National Union's conduct was sufficiently reprehensible to merit the imposition of punitive damages, the court also notes, as did the Supreme Court in *BMW*, that the harm inflicted was purely economic in nature. Nothing done by the defendant showed any "indifference to or reckless disregard for the health or safety of others." *BMW* at 5750. This factor has also been used by California courts in the process of assessing the reprehensibility of the defendant's conduct when reviewing a punitive damage award. For example, the court in *Seeley* v. *Seymour*, 190 Cal.App.3d 844, 867 (1987) observed that the parties in that case were sophisticated businessmen of relatively equal bargaining strength, and thus the situation carried "a lesser degree of 'reprehensibility'" than the more typical punitive damage case where a large or sophisticated business enterprise uses its wealth or power to exploit the weak or the unwary. *Id.* The court concludes that in this case as well, the parties were

both large business enterprises, neither of which was able to exploit the other.

The second *BMW* guidepost is the ratio of the punitive damages to the actual harm. This factor has been addressed above under California law. The U.S. Supreme Court has stated that it is impossible to "draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable that would fit every case." The Court reiterated, however, that a "general concern of reasonableness properly enters into the constitutional calculus." As noted above, this court concludes that a ratio of 60 to 1 raises a presumption of jury passion or prejudice. Consistent with a "general concern of reasonableness," the court also concludes that permitting this award to stand would make it constitutionally suspect.

The third *BMW* guidepost is a consideration of sanctions adopted by the legislature for comparable misconduct. National Union points to Insurance Code 790.035(a) which imposes a penalty of up to $10,000 for each act in violation of section 790.03. While this court has concluded that the punitive damage award is excessive for the other reasons stated above, the utilization of section 790.035(a) as a guidepost is of significantly less importance. It is noted that the "guideposts" reviewed by the Supreme Court were all for the purpose of assisting the Court in determining whether the defendant received "fair notice not only of the conduct that will subject [it] to punishment but also of the severity of the penalty that a State may impose." *BMW* at 5750. Despite the civil penalties provided by Section 790.035, California has a long history of permitting punitive damage awards where the evidence is sufficient to establish fraud or the malicious or oppressive breach of the covenant of good faith and fair dealing. Surely National Union does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law. It is also significant to observe in this connection that despite the long history of these awards under the common law, the

California legislature has not acted to impose any statutory limitation on such awards as it has, for example, with respect to negligence actions against health providers.

Accordingly, as noted at the outset, the court concludes that the punitive damage award in this case is excessive. Because the same jury must determine both punitive damages and liability, *Medo* v. *Superior Court*, 205 Cal.App.3d 64, 66-68 (1988), a new trial is ordered on the causes of action for fraud, breach of the covenant of good faith and fair dealing, and on the award of punitive damages. The new trial will be as to National Union only. The court has determined from the evidence, however, that an award of $1.7 million for punitive damages would be fair and reasonable. Therefore, if plaintiff files its written consent to reduce the award of punitive damages to the amount of $1.7 million, the motion for new trial will be denied. CCP 662.5. Plaintiff's written consent to the remittitur, should it choose to do so, is to be filed and served within 15 days of the date of this order.

Clerk to give notice to the parties

DATED: July 29, 1996

/s/ Raymond J. Ikola
RAYMOND J. IKOLA,
Judge of the Superior Court

APPENDIX D

SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF ORANGE

Case No. 734096

TEXTRON FINANCIAL CORPORATION, A DELAWARE CORPORATION,

Plaintiff,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA; AND AMERICAN INTERNATIONAL ADJUSTMENT COMPANY, INC.,

Defendant.

Assigned for All Purposes to:
Judge Raymond J. Ikola
Dept. 8

Filed: August 12, 1996

TEXTRON'S WRITTEN CONSENT
TO REMITTITUR OF PUNITIVE DAMAGES

TO ALL PARTIES AND TO THEIR ATTORNEYS OF RECORD:

PLEASE TAKE NOTICE that Textron Financial Corporation ("Textron") consents to the remittitur of punitive damages from $10 million to $1.7 million, in accordance with the Court's ruling and order conditionally granting National Union's motion for a new trial (which was filed on July 29, 1996).

DATED: August 12, 1996

BERGER, KAHN, SHAFTON, MOSS,
FIGLER, SIMON & GLADSTONE
A Professional Corporation

By: /s/ David B. Ezra
DAVID B. EZRA,
Attorneys for Plaintiff TEXTRON
FINANCIAL CORPORATION

APPENDIX E

COURT OF APPEAL, FIRST APPELLATE DISTRICT,
DIVISION FOUR - NO. G020323

IN THE SUPREME COURT OF CALIFORNIA

En Banc

S095924

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PENNSYLVANIA ET AL.,
Defendants and Appellants.

Filed: May 2, 2001

Petition for review DENIED.

GEORGE
Chief Justice

APPENDIX F

COURT OF APPEAL, FOURTH APPELLATE DISTRICT,
DIVISION THREE - NO. G020323

IN THE SUPREME COURT OF CALIFORNIA

En Banc

S095924

TEXTRON FINANCIAL CORPORATION,
Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PENNSYLVANIA ET AL.,
Defendants and Appellants.

Filed: May 4, 2001

The order filed on May 2, 2001, is hereby modified to reflect the above-captioned corrected district and division.

/s/ George
Chief Justice

Supreme Court, U.S.
FILED
AUG 29 2001
OFFICE OF THE CLERK

No. 01-176

In The

Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

v.

TEXTRON FINANCIAL CORPORATION,

Respondent.

On Petition For Writ Of Certiorari To The California Court Of Appeal, Fourth Appellate District

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Where a state appellate rule provides that a state supreme court will not consider an issue omitted from an intermediate court's opinion unless brought to the attention of the intermediate court in a petition for rehearing, and where a party did not assert in such a petition that the intermediate court failed to explicitly mention one of the "guideposts" in reviewing a punitive damages award under *BMW of North American v. Gore*, 517 U.S. 559 (1996), has the party waived that issue when it unsuccessfully seeks review in the state supreme court and then seeks certiorari in this Court?

2. Where a state trial court reduces a punitive damages award from $10 million to $1.7 million, and where the defendant attempts to defend such a remittitur in a reviewing court by arguing that the trial court did not abuse its discretion, has the defendant invited the reviewing court to affirm the award as remitted under an abuse of discretion standard, thus precluding an argument in this Court that a de novo standard should be applied?

3. Where a state reviewing court discusses and applies both state and federal authorities and concludes that a punitive damages award "is permissible under both state and federal law," are there grounds to grant certiorari to review such an award?

4. Assuming that the California Court of Appeal in this case applied an abuse of discretion standard in reviewing the punitive damages award and assuming

QUESTIONS PRESENTED – Continued

that petitioner did not waive the issue or invite the error, would application of a different standard of review result in a different judgment?

5. Assuming the California Co of Appeal failed to independently review federal law standards pertaining to punitive damages, is reinstatement of the jury's original $10 million award required as a matter of constitutional law?

TEXTRON'S RULE 29.6 STATEMENT

Textron Financial Corporation is a wholly-owned subsidiary of Textron, Inc.

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INTRODUCTION

This case involved an insurance company that fabricated policy documents after a loss to fraudulently and retroactively remove insurance coverage.

In its petition, National Union likens this case to *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. ___, 121 S.Ct. 1678 (2001). But this case was not like *Cooper*. In this case, a California jury found that an insurance company that was duty-bound to act with utmost good faith did just the opposite – committing insurance fraud and insurance bad faith. Contrary to National Union's repeated assertions, no court ever "rubber-stamped" that jury's verdict. In fact, the California judiciary took just the opposite approach, affirmatively using the federal constitution to slash the jury's punitive damages verdict by 83 percent. In contrast to *Cooper*, no level of the California judiciary ever refused to examine or evaluate the constitutional propriety of the jury's verdict. At every level of review, the California judiciary insisted that federal constitutional principles called for a significant reduction of the jury's verdict.

As it did throughout the appellate process, National Union continues to view the facts of the case as if it prevailed at trial. If the actual facts of this case were anything close to those that National Union continues to argue, the jury would have found in favor of National Union, not against it.

Trying to generate a federal issue where none exists, National Union offers a distorted reading of the Court of Appeal's opinion. The Court of Appeal's opinion actually reflects that it independently evaluated federal constitutional punitive damages law not once, but twice.

In the pages that follow, Textron points out some of the major problems with National Union's petition.

Among other things, National Union waived the belated argument that it advances in this petition. When it petitioned for rehearing with the Court of Appeal that issued the challenged opinion, National Union did not raise the standard of review issue. Under California law, the standard of review issue had to be raised in the petition for rehearing if National Union was to maintain a right to seek further review on that basis.

And National Union invited the very "error" that it now complains about. Ironically, when it briefed these issues in the California Court of Appeal, National Union advocated an abuse of discretion standard, arguing that "no abuse of discretion occurred here," and that the trial court "did not abuse its discretion in holding that the jury's $10 million punitive damage award was excessive." App. 41-42.[1]

Ultimately, this case doesn't just involve a questionable paint job or a 500 to 1 ratio of punitive to compensatory damages. The issue raised in National Union's petition has no merit and does not warrant further judicial review.

FACTUAL BACKGROUND

This trial lasted more than a month and a half, and generated a record that exceeded 10,000 pages. On appeal, the parties filed various augmentations of the record, several motions, and seven separate appellate briefs that occupied over 300 pages and raised numerous legal and factual arguments.

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[1] Citations to respondent's appendix are abbreviated "App." Citations to petitioner's appendix are abbreviated as PA [page no.]a.

Textron's task of presenting the facts is made more difficult because National Union's petition presents an incomplete and misleading version of the facts.

In early 1992, Textron loaned Il Sung Ko $87,000 to buy a tour bus for his business. To protect itself, Textron had Ko obtain insurance covering Textron's security interest in the bus. Ko bought insurance from National Union. Textron was named as an additional insured under the policy. PA 3a.

After the 1992 Los Angeles riots, Ko faced a slowing tourism business and cash flow problems. Douglas Ferguson, Ko's broker, advanced a premium payment for Ko. Nevertheless, on October 22, 1992, National Union sent Ko a cancellation notice which said the policy would cancel as of November 27, 1992. PA 3a.

Aware that Ko was not using some of the six buses in his fleet, Ferguson wrote to TRM International, Inc., National Union's managing general agent for bus insurance, and asked if a new policy could be issued "with only four units." In response to Ferguson's inquiry, George Peare, a TRM underwriter, responded by suggesting a lay-up credit, a "much easier way of doing it." PA 3a. According to Ferguson, discussion about the lay-up credit was limited. He was told to "Get the license plates. Get the license plates."

Lay-up credits are a form of mileage rating. The risk of loss is reduced where fewer total miles are being driven. So an insurer that offers a lay-up credit reduces the premium when vehicles are not in regular use. Unlike deletions, lay-up credits do not eliminate or even reduce coverage. Because full coverage remains in effect, insurance companies that issue lay-up credits typically ask for

license plates to minimize the likelihood that a laid-up vehicle will be used on a daily basis. PA 4a.[2]

The lay-up credit was advantageous for National Union since it kept the policy in force, allowed National Union to continue collecting premium payments of about $5,000 a month, required very little paperwork, and did not require notice to other parties. In contrast, vehicle deletions would have required notice to Textron, other lenders, various public entities, and the City of Los Angeles.

A few days after the policy was canceled for nonpayment of premium (without notice to Textron), Ko made a partial premium payment and sent the license plates for two of his six buses to Ferguson. Within a few days, National Union implemented the lay-up credit, and the policy was reinstated in full, with no reduction in coverage. PA 4a.

Ko's broker, Ferguson, did not understand the difference between lay-up credits and deletions. Ferguson thought lay-up credits and deletions were the same thing. He incorrectly assumed that lay-up credits and suspensions terminated coverage.

Ferguson also wanted to make sure he recovered the premium he had advanced. So after National Union reinstated the policy, Ferguson continued to send notes to TRM which emphasized that he had the license plates. However, since the lay-up credit had already been issued,

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[2] "Deletions," on the other hand, eliminate coverage for the deleted vehicle. As a result, policyholders are not required to turn in license plates when the insurer deletes a vehicle from coverage. Deletions typically occur when a policyholder sells a vehicle to a third party. If insurance companies made policyholders turn in license plates when coverage was deleted, policyholders would not be able to sell their vehicles.

and the policy fully reinstated, TRM did not bother to respond.

On January 7, 1993, one of Ko's buses broke down. The Textron-financed bus was sent to pick up stranded passengers, and it was severely damaged when it spun on a patch of ice and collided with a truck. Since Ferguson erroneously believed lay-up credits eliminated coverage, he told Ko (and Ko's assistant) the accident was not covered. Nevertheless, after talking to a TRM claims supervisor, Dick Longuil, Ferguson presented a claim to National Union (through its adjusting affiliate, American International Adjustment Company (AIAC)). PA 4a.

Because the lay-up credit had resulted in a full policy reinstatement, coverage for the accident was internally verified on February 4, 1993. PA 4a. But a claims adjuster subsequently spoke to Ko's assistant and learned that Ko and his assistant (neither of whom spoke English as a first language) erroneously believed there was no coverage for the accident. The adjuster did not disclose that coverage had already been verified, explaining that "coverage is usually, in my experience, only discussed with an insured if it's a problem."

Claims adjusters had been instructed to contact John Lavin (an underwriting manager in National Union's Home Office) "for a complete policy copy." The claims office did request a copy of the policy, but National Union refused to release the policy, even to its own adjusters.

Because National Union's Home Office refused to allow access to the actual policy, claims personnel turned to the TRM claims supervisor, Dick Longuil. But Longuil worked in New York, eight hours away from TRM's New Jersey office. As a result, Longuil did not have access to any file materials.

Even without documents, however, Longuil immediately had "a bad feeling about" the accident. He was troubled by the possibility of personal injury claims that could become very costly for the insurer if the bus was carrying passengers. (Even as late as September of 1994, National Union Home Office personnel were still worried about "potential B[odily] I[njury] claims").

A few days later, National Union denied Ko's claim (and the claim that had been presented for the owner of the truck that was hit by the bus). National Union said coverage had been canceled before the accident. PA 4a. The claims were denied even though coverage had been internally verified, even though the policy had been fully reinstated before the accident, and even though there were no policy documents or computer records showing a "deletion."

As of February 1993, no one had told Textron about the policy cancellation, the lay-up credit, the policy reinstatement, the accident, or the coverage verification.

Ko continued making loan payments as long as he could. But by late 1993, Ko defaulted on his Textron loan. Textron then learned the bus was involved in an accident earlier that year. When it inquired, Textron was falsely told its bus coverage was terminated before the accident. As a result, Textron was required to sue Ko, who was forced into bankruptcy. PA 4a.

National Union formally denied Textron's claim based on the false contention that National Union couldn't tell Textron about the coverage termination because National Union itself did not have advance notice of the cancellation. National Union's denial letter did not disclose the lay-up credit, the reinstatement, or the fact that coverage had been verified after the accident.

Textron had started asking for a copy of the National Union insurance policy in January 1994. Two months later, in March 1994, National Union finally gave its own claims adjusters a copy of the original Home Office policy. But National Union decided to withhold the policy from Textron. Why did National Union refuse to let Textron see a copy of the original policy? Because the original policy had a credit endorsement, but no "deletion" endorsement.

Rather than giving Textron a copy of the original policy, National Union waited another five months and then it gave Textron a different version of the policy. This new version of the policy conveniently replaced the credit endorsement No. 8 with a falsified "deletion" endorsement No. 8 – a falsified document that had been created long after the accident. PA 4a.

Textron sued National Union in August 1994. By the end of the trial, everyone in the courtroom knew that National Union had been caught perpetrating a serious fraud. National Union had issued a lay-up credit and fully reinstated the policy *before* the accident. But because it was worried about a flood of possible personal injury claims that might have come from passengers on a seriously damaged tour bus, and because it knew Ko and his broker did not know about lay-up credits, National Union had fabricated certain documents and concealed others to fraudulently and retroactively terminate coverage. App. 23.

National Union's own designated claims handling expert testified about two other California cases where National Union had misled policyholders and been subjected to substantial punitive damages awards ($43 million and $14 million). In one of those cases, National

Union had even taken steps to retroactively reduce coverage. App. 29. National Union's witnesses admitted that the company had a corporate policy of not apologizing to its policyholders. App. 30.

From start to finish National Union tried to conceal evidence and deceive Textron and others. When it started responding to Textron's claim, National Union chose not to mention important facts, such as the fact that the policy had been fully reinstated before the accident. To prevent Textron from learning that the fabricated deletion endorsement had been created after the accident, a "certificate of mailing" was placed over the purported creation date before the falsified "deletion" version of endorsement No. 8 was faxed to Textron. App. 27-28.[3]

Then, instead of giving Textron a copy of the actual policy, National Union gave Textron a different version of the policy – a version which substituted a fabricated "deletion" endorsement for the lay-up credit endorsement. The original policy was withheld until a court ordered it to be produced, because National Union knew the original policy revealed that as late as October of 1993 (nine months after the accident) there was still no "deletion" endorsement. App. 27.

During trial, the jury also learned that National Union's underwriting file had been manipulated before it was produced to Textron. The file manipulation was exposed because Ferguson's file included lay-up credit-related correspondence that had been removed from the

---

[3] The "certificate of mailing" revealed further efforts to deceive. For example, there was no corresponding "certificate of mailing" for the other bus that was supposedly "deleted." If National Union had been providing routine "deletion" notices, it would have prepared "certificates of mailing" for both buses, not just the Textron-financed bus.

underwriting file. For example, Exhibit 15 was the underwriter's "much easier way of doing it" letter. The "much easier way of doing it" obviously referred to a lay-up credit. But Exhibit 15 (and other similar documents) had been removed from the underwriting file before the file was produced to Textron. App. 26.

During trial, National Union went so far as to destroy documents to keep them from the jury. For example, National Union's Portland claim file was housed in a jacket that would have reflected important claims information. Nevertheless, National Union produced only part of the file, explaining that "some idiot" had destroyed the file's jacket before it could be made available to Textron. There was no legitimate reason to destroy the jacket. In fact, without the jacket, there was nothing to hold the file together. App. 26.

Attempts to deceive continued right up to the last day of trial, when National Union called a witness who tried to get the jury to believe Textron had been paid (or soon would be paid in response to the jury's decision). But National Union never made any voluntary payment to Textron.

The evidence permitted only one reasonable conclusion: that National Union had perpetrated a serious fraud and then tried to cover it up. In fact, the conduct was so egregious that even National Union's own attorney conceded during closing arguments that if the jury believed the documents rather than National Union's witnesses, then this conduct was "vile." App. 26.

In addition to insurance bad faith, the jury's verdict found fraud by National Union. The findings included both affirmative misrepresentation and concealment. Applying California's heightened clear and convincing

evidence standard, the jury also found that National Union acted with malice, with fraud *and* with oppression.

The trial judge reached the same conclusion on post-trial motions, affirming the jury's conclusion that National Union perpetrated a fraud.

POST-TRIAL PROCEDURAL HISTORY

Following trial and entry of judgment, National Union moved for a new trial and asked the trial judge to reduce the jury's verdict based on *BMW v. Gore*, 517 U.S. 559 (1996). Ironically, the trial judge reduced the jury's punitive damages verdict from $10 million to $1.7 million, despite observing that:

> California has a long history of permitting punitive damage awards where the evidence is sufficient to establish fraud or the malicious or oppressive breach of the covenant of good faith and fair dealing. *Surely National Union does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law.*

PA 39a, italics added.

When it appealed the ruling, National Union made a wide array of sometimes contradictory arguments that substantially evolved and changed over time. National Union started with a laundry list of arguments centered squarely on state law issues – such as jury instructions pertaining to the state law definition of a "managing agent," common law principles of "offset" and ratification, and various state law standards for tort liability. App. 3-4.

In the very last part of its 65-page opening brief, National Union argued that *BMW v. Gore* mandated further reduction of the already substantially reduced punitive damages award. But National Union did not argue that it lacked fair notice that it could be subjected to a multi-million dollar punitive damages award if it was caught fabricating policy documents after a loss in order to fraudulently deny an insurance claim. It simply used its own erroneous view of the facts to argue the *BMW* guideposts without reference to their ultimate function. App. 5-12.

In a subsequent appellate brief, National Union prioritized its arguments for the Court of Appeal. National Union unequivocally said a single state law issue was of paramount importance, explaining that:

> The principal issue on this appeal is whether the trial court erred by instructing that TRM was National Union's managing agent under Civil Code section 3294.

App. 39.

Ironically, in that same brief, National Union urged the Court of Appeal to apply an abuse of discretion standard to the $1.7 million punitive damages award – a position that seems to be exactly the opposite of the position National Union is advancing in this petition. App. 41-42.

In its unpublished opinion, the Court of Appeal disposed of a wide array of issues that had been raised in National Union's appeal, Textron's separate appeal, and Textron's cross-appeal. The Court of Appeal's opinion did not address each and every sub-part of every argument that had been advanced by Textron and National Union in their 300+ pages of briefing. Of course, an opinion that extensive would have required several hundred pages of discussion.

Following the issuance of the appellate opinion, National Union petitioned for rehearing with the California Court of Appeal, as it was required to do under state law in order to preserve issues for further review. However, National Union's petition for rehearing did *not* address the standard of review, and it never argued that the Court of Appeal failed to independently consider federal constitutional principles pertinent to punitive damages. App. 50-53. The petition for rehearing was denied, as was National Union's petition for review to the California Supreme Court.

REASONS WHY NATIONAL UNION'S PETITION SHOULD BE DENIED

National Union does not argue that this case satisfies the traditional and accepted standards for invoking this Court's discretionary review. Indeed, this was an unpublished appellate court decision followed by a summary denial of review in the state's supreme court.

In addition to the fact that there is no legitimate reason for this Court to consider National Union's petition, there are many other problems with National Union's petition. Some of these problems are discussed below.

1. NATIONAL UNION WAIVED THE ONE ARGUMENT ADVANCED IN ITS PETITION

Under California law, National Union was required to raise the standard of review issue in a petition for rehearing with the court of appeal that decided the case if it wanted to preserve that issue for further appellate review. Rule 29(b) of the California Rules of Court provides in pertinent part:

> As a matter of policy, on petition for review the Supreme Court normally will not consider . . . any issue or any material fact that was omitted from or misstated in the opinion of the Court of Appeal, unless the omission or misstatement was called to the attention of the Court of Appeal in a petition for rehearing.

National Union filed a petition for rehearing, but the petition did not raise the standard of review issue. Instead, National Union's petition for rehearing simply reargued various factual positions that it had unsuccessfully argued during the trial. App. 50-53.

Because National Union failed to properly preserve the standard of review argument for further review, the argument was waived in the California Supreme Court, and it is waived here.

As this Court has held, "we will not consider a petitioner's federal claim unless it was either addressed by, or properly presented to, the state court that rendered the decision we have been asked to review." *Adams v. Robertson*, 520 U.S. 83, 86 (1997). To properly preserve an argument for potential review, a petitioner must establish that the claim was raised "at the time and in the manner required by the state law." *Bankers Life & Cas. Co. v. Crenshaw*, 486 U.S. 71, 78 (1988) (quoting from *Webb v. Webb*, 451 U.S. 493, 501 (1981)).

National Union's petition boils down to a single argument – that the California Court of Appeal should have written a longer opinion – one that included two extra sentences: a sentence saying National Union's conduct fell at the extreme end of the reprehensibility scale and a sentence saying insurance fraud merits substantial civil or criminal penalties.

These issues were fully briefed and evaluated by the Court of Appeal. App. 5-12, 15-30, 33-35, 41-42, & 46-49.

But to the extent National Union took issue with the Court of Appeal's opinion, National Union had to petition for rehearing on that basis in order to give that same panel of judges a chance to correct the error National Union perceived. National Union's failure to raise the standard of review issue in its petition for rehearing resulted in a waiver of National Union's argument.

2. NATIONAL UNION INVITED ANY PERCEIVED ERROR

A fair reading of the Court of Appeal's opinion reflects that the court independently evaluated federal constitutional punitive damages constraints twice – once in connection with Textron's argument that the $10 million verdict was appropriate under federal law, and then again when rejecting National Union's argument that the substantially reduced $1.7 million award was unconstitutional.

In *Cooper Industries v. Leatherman Tool Group, Inc.*, 532 U.S. ___, 121 S.Ct. 1678 (2001), this Court held that in evaluating the propriety of a jury verdict awarding punitive damages, an appellate court should exercise independent review with respect to the federal constitution's due process limits on punitive damages, and it should not apply an abuse of discretion standard. 121 S.Ct. at 1688.

Ironically, in its briefing to the Court of Appeal, National Union itself urged the court to apply an abuse of discretion standard.[4] So even if the California Court of

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[4] Among other things, National Union argued that "[n]o abuse of discretion occurred here." App. 41. And National Union argued that the trial court "did not abuse its discretion in holding that the jury's $10 million punitive damage award was excessive." App. 42.

Appeal had applied an abuse of discretion standard, and even if it had not independently evaluated federal constitutional issues, there would still be no basis for further review by this Court. This is because when it urged the Court of Appeal to adopt an abuse of discretion standard, National Union invited the alleged "error" that it is complaining about now.

Where a party invites a court to commit error in California, the party is estopped from asserting that alleged error as a ground for reversal on appeal. *See, e.g., Norgart v. Upjohn Co.*, 21 Cal.4th 383, 403 [981 P.2d 79, 92] [87 Cal.Rptr.2d 453, 467] (1999) and *Hasson v. Ford Motor Co.*, 32 Cal.3d 388, 420-21 [650 P.2d 1171, 1191] [185 Cal.Rptr. 654, 674] (1982), *cert. dismissed*, 459 U.S. 1190 (1983).

To argue against the appellate court's reinstatement of the jury's $10 million punitive damages verdict, National Union urged the appellate court to apply an abuse of discretion standard to the punitive damages award. Therefore, even if the Court of Appeal had applied an abuse of discretion standard (which it did not), National Union invited that alleged error and waived the right to challenge the Court of Appeal's decision on that basis.

3. THE CALIFORNIA COURT OF APPEAL INDEPENDENTLY REVIEWED FEDERAL CONSTITUTIONAL PUNITIVE DAMAGES STANDARDS

In its effort to suggest that the California Court of Appeal ignored federal punitive damages standards, National Union selectively quotes a few sentences from the opinion dealing with California's own state law standards for punitive damages review, and conveniently ignores language in the opinion dealing with the court's

separate analysis of the applicable federal law standards. Actually, the Court of Appeal evaluated *both* state and federal punitive damages law.

Since 1988, California has imposed stringent safeguards against unwarranted punitive damages awards. For example, under applicable state law, a defendant can (and in this case did) request a bifurcated trial, so that the jury must decide liability *and* malice, fraud or oppression before it hears about the defendant's wealth. Cal. Civ. Code § 3295(d). Punitive damages are only recoverable on a showing of malice, fraud, or oppression. Cal. Civ. Code § 3294(a).

To establish malice or oppression, a plaintiff needs to establish despicable conduct. Cal. Civ. Code § 3294(c). Consistent with current California law, the jury that decided this case was instructed that "despicable conduct" is "conduct which is so vile, base, contemptible, miserable, wretched, or loathsome that it would be looked down upon and despised by ordinary decent people."

And perhaps most importantly, since 1988, California law has only permitted punitive damages if the jury determines that malice, oppression, and fraud has been proven by "clear and convincing" evidence. Cal. Civ. Code § 3294(a). In this case, consistent with current California law, the jury was instructed that "clear and convincing evidence" means evidence "so clear as to leave no substantial doubt; sufficiently strong to command the unhesitating assent of every reasonable mind."

The jury's findings were based on its assessment of witness credibility and evidence that demonstrated a pattern of deceit and deception by an insurance company that had an obligation to act with utmost good faith

toward Textron and others. National Union then compounded the wrongdoing by trying to cover it up, and going so far as to remove key documents from files (and destroying other documents).

Under state law standards for punitive damages, the $10 million verdict posed no problems. The reprehensibility of the conduct was extreme, and it was compounded by National Union's efforts to cover it up and evidence of National Union's recidivism. National Union's wealth was obviously significant (almost $4 billion). Finally, as compared to the amount of compensatory damages the trial judge allowed, the 60:1 ratio was far less than other awards that have been approved by state and federal courts. And when the potential harm was considered, the ratio became something closer to 1:1.

A. California Punitive Damages Review Involves An Assessment Of Whether The Jury Acted Based On Passion And Prejudice

When assessing a jury's punitive damages verdict under state law, California courts "historically honored [the] standard of reversing as excessive only those judgments which the entire record, when viewed most favorably to the judgment, indicates were rendered as the result of passion and prejudice on the part of the jurors." *Bertero v. National General Corp.*, 13 Cal.3d 43, 65 fn. 12 [529 P.2d 608, 624, 118 Cal.Rptr. 184, 200] (1974).

In assessing whether or not a particular jury's verdict was based on passion or prejudice, California courts typically analyzed the "varying degrees of reprehensibility," the ratio between punitive damages and compensatory damages, and "the wealth of the particular defendant." *Neal v. Farmers Ins. Exchange*, 21 Cal.3d 910, 928 [528 P.2d 980, 990, 148 Cal.Rptr. 389, 399] (1978).

This state law standard required an assessment of the particular facts of each case, with the appellate court trying to determine whether or not the jury's verdict was improperly based on passion and prejudice.

Two cases decided before California implemented the current laws that make it much harder to get punitive damages illustrate the point. In *Rosener v. Sears, Roebuck & Co.*, 110 Cal.App.3d 740 [168 Cal.Rptr. 237] (1980), *appeal dismissed*, 450 U.S. 1051 (1988), a $10 million punitive damages award was reversed in a case where the evidence established that "shoddy workmanship" resulted in injuries "varying from the loss of a family Bible caused by leaks in an unrepaired roof, to the total loss of privacy suffered by an entire family forced to sleep in the same room when the interior walls of their room were left unrepaired." 110 Cal.App.3d at 747 [168 Cal.Rptr. at 241]. In *Rosener*, the court decided that the jury acted based on passion or prejudice, particularly since the trial court failed to instruct the jury that the punitive damages award had to be reasonably related to the amount of harm inflicted by the defendant. 110 Cal.App.3d at 753-54 [168 Cal.Rptr. at 254].

At the opposite end of the spectrum is *Downey Savings & Loan Assoc. v. Ohio Cas. Ins. Co.*, 189 Cal.App.3d 1072 [234 Cal.Rptr. 835] (1987), *cert. denied*, 486 U.S. 1036 (1988). Like this case, *Downey Savings* involved an insurance company that failed to honor its duty of good faith and fair dealing. And like this case, the plaintiff in *Downey Savings* was a successful business enterprise, not an individual or family likely to generate undue sympathy. Although there was no evidence of overt fraud, the insurance company had failed "to give the interests of the insured at least as much consideration as it gives to its own interests." 189 Cal.App.3d at 1098 [234 Cal.Rptr. at

850]. In approving a $5 million punitive damages verdict (against $152,000 in compensatory damages), the *Downey Savings* court zeroed in on California's passion or prejudice standard, noting that "the plaintiff here was not one to arouse the jury's sympathy." 189 Cal.App.3d at 1099 [234 Cal.Rptr. at 850].

In this case, the state's standard for assessing punitive damages did not require any modification of the jury's $10 million punitive damages verdict. The reprehensibility of the conduct was extreme, to say the least. National Union's wealth was far larger than other defendants who had received similar or greater punishments. And the ratio of punitive damages to the harm or potential harm associated with National Union's conduct was substantially less than other ratios that had been affirmed by California courts.

Most importantly, however, this was never a case where a jury would ever be tempted to act based on passion and prejudice. From the first day of the trial forward, National Union repeatedly reminded the jury that Textron was an out-of-state corporation that had substantial assets, and whose corporate parent was at one time a Fortune 50 company. Instead of being based on sympathy for Textron or passion and prejudice against a large corporation, the jury's punitive damage assessment recognized the extreme reprehensibility of National Union's conduct, its fraudulent retroactive efforts to deny coverage, its total lack of remorse, and its unrelenting efforts to conceal its wrongdoing.

B. Federal Punitive Damages Law Focuses On Adequate Notice To The Defendant

Federal punitive damages law does not focus on passion and prejudice of a jury. To the contrary, "the

federal excessiveness inquiry appropriately begins with an identification of the state interests that a punitive award is designed to serve." *BMW*, 517 U.S. at 568. And the three *BMW* guideposts are intended to assess the question of whether or not a defendant has "fair notice . . . of the severity of the penalty that a State may impose." *Id.* at 574.

C. The California Court Of Appeal's Opinion

The California Court of Appeal that decided this case was well aware of the differing federal and state law standards for punitive damages review. In contrast to the federal appellate court that decided *Cooper*, the California Court of Appeal here did *not* apply an abuse of discretion standard.[5] And unlike the intermediate appellate court whose decision was at issue in *San Paolo U.S. Holding Co., Inc. v. Simon*, 532 U.S. ___, 121 S.Ct. 2190 (2001), the Court of Appeal here did not fail to appreciate the differences between federal and state punitive damages law.[6]

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[5] The federal appellate court that decided *Cooper* did not independently analyze federal law constraints on punitive damages because it simply determined that "the district court did not abuse its discretion in declining to reduce the amount of punitive damages." *Leatherman Tool Group, Inc. v. Cooper Industries, Inc.*, 205 F.3d 1351, 1999 WL 1216844, at *2 (9th Cir. 1999).

[6] In *Simon*, the appellate court that refused to reduce a $1.7 million punitive damages award that had been rendered against a compensatory award of $5,000, declined to analyze federal law by saying that, "[t]he *BMW* guidelines are nearly identical, and serve the same purpose as California's criteria; thus, an award which passes muster under California's rules will satisfy the requirements for federal due process." *Simon v. San Paolo U.S. Holding Co., Inc.*, Case No. B121917 (reprinted in *San Paolo*, No. 00-1457, Pet. App. A-28).

The Court of Appeal here appropriately devoted the majority of its attention to National Union's primary arguments, rather than the very last argument National Union raised in its 135 pages of briefing. Nevertheless, the Court of Appeal independently determined that the trial judge had properly analyzed *BMW* and federal constitutional law to cut the jury's $10 million punitive damages verdict to $1.7 million. PA 23a.

Then the Court of Appeal analyzed National Union's argument against the reduced award. After addressing the state law "passion and prejudice" standard, the court turned to its independent analysis of federal law. The court specifically acknowledged *BMW*'s three guideposts, and their focus on whether or not the defendant had fair notice that its conduct could result in the challenged punitive damages award. PA 24a.

After specifically acknowledging the three guideposts, the California Court of Appeal independently concluded that the "record reflects the present award is permissible under *both* state and federal law." PA 24a.

Since the Court of Appeal's opinion reflects that it was aware of the differences between federal and state punitive damages law, and because the opinion reflects that federal law issues were independently reviewed, National Union cites to a series of cases that pre-date this Court's *BMW* decision.

The cases that were decided between 1949 and 1990 do not involve *any* assessment of federal constitutional issues pertaining to punitive damages. For example, in *Neal v. Farmers Ins. Exchange*, 21 Cal.3d 910 [582 P.2d 980, 148 Cal.Rptr. 389] (1978), the defendant never challenged punitive damages on the basis of any constitutional argument. Instead, the defendant argued that it had done

nothing wrong, and that there was no evidence to support the verdict. 21 Cal.3d at 921-22 [582 P.2d at 985-986, 148 Cal.Rptr. at 493-95]. As a result, the court focused on state law standards that addressed jury passion and prejudice.

National Union does cite two more recent cases. In *Shade Foods, Inc. v. Innovative Product Sales & Marketing, Inc.*, 78 Cal.App.4th 847, 909-910 [93 Cal.Rptr. 2d 364, 395-396] (2000), the court applied the more stringent punitive damages standards California implemented in 1988 to reverse the punitive damages award, finding that the record would not support a finding of malice and oppression by clear and convincing evidence.[7] Accordingly, there was no need to even consider federal constitutional issues. Likewise, in *Lane v. Hughes Aircraft Co.*, 22 Cal.4th 405 [993 P.2d 388, 93 Cal.Rptr. 2d 60] (2000), there is no indication that either party raised issues concerning federal constitutional limits on punitive damages.

Although National Union's petition never mentions it, California law requires independent review of constitutional issues. *See, e.g.*, EISENBERG, HORVITZ & WIENER, CIVIL APPEALS & WRITS: CALIFORNIA PRACTICE GUIDE § 8:110.1 (2000) ("constitutional issues (due process or equal protection challenges, etc.) are reviewed de novo"). In this regard, the Court of Appeal's independent review was consistent with many other California decisions. *See, e.g., Aguilar v. Atlantic Richfield Co.*, 25 Cal.4th 826, 860 [24

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[7] Since 1988, California appellate courts have used these changes in California punitive damages law to strike down a punitive damages verdict in cases where the record failed to establish wrongdoing that could fairly be described as "despicable conduct." *See, e.g., Mock v. Michigan Millers Mutual Ins. Co.*, 4 Cal.App.4th 306, 328-333 [5 Cal.Rptr.2d 594, 607-610] (1992).

P.3d 493, 517, 107 Cal.Rptr. 2d 841, 870] (2001) (a court's application of facts to decisional law "is itself scrutinized de novo"); *State of Ohio v. Barron*, 52 Cal.App.4th 62, 67 [60 Cal.Rptr.2d 342, 344] (1997) ("As correctly noted by defendant, constitutional issues are reviewed de novo."); and *Mohilef v. Janovici*, 51 Cal.App.4th 267, 285 [58 Cal.Rptr.2d 721, 730] (1996) (holding that where the issue involves "application of the due process clause, we review the trial court's decision de novo").

Contrary to National Union's implied suggestion, California courts independently review due process determinations.

Nothing in the Court of Appeal's discussion of *BMW* suggests that the court failed to independently consider federal law issues. And nothing in the opinion suggests that the court applied an abuse of discretion standard to its assessment of federal law punitive damages constraints.

National Union's petition is based on the erroneous assumption that the Court of Appeal never evaluated federal law punitive damages standards.

4. EVEN IF THE CALIFORNIA COURT OF APPEAL ANALYZED FEDERAL LAW PERTAINING TO PUNITIVE DAMAGES UNDER AN ABUSE OF DISCRETION STANDARD, THE ALREADY SUBSTANTIALLY REDUCED $1.7 MILLION PUNITIVE DAMAGES AWARD WOULD NOT BE INVALID

In *Cooper*, this Court seemed to acknowledge that the applicable standard of review may "affect the result of the *Gore* analysis in only a relatively small number of cases." 532 U.S. at ___, 121 S.Ct. at 1688. However, in *Cooper* the standard of review could have been significant because the jury had been inappropriately told that it

could punish the defendant for perfectly legal conduct: copying the functional features of an unpatented product. The fact that the jury had awarded a $4.5 million punitive damages verdict against a $50,000 compensatory damages award (a 90:1 ratio) was sufficient to raise a constitutional issue, particularly since it appeared that the jury had punished the defendant for lawful conduct.

This problem – the possibility that a defendant was punished for perfectly legal conduct – was also identified in *BMW*. In fact, *BMW*'s conduct was perfectly legal in "roughly 25 States." 517 U.S. at 565.

In contrast to cases like *Cooper* and *BMW*, this case involved deliberate insurance fraud, in addition to insurance bad faith. National Union has never argued that insurance fraud is legal in any state. Instead, insurance fraud is typically considered a crime of such magnitude that it warrants substantial imprisonment, in addition to large fines. For example, in California, insurance fraud penalties include five (5) years *imprisonment* and fines of up to "double the value of the fraud." Cal. Penal Code § 550(b).

National Union never addressed the fact that its conduct was illegal everywhere (and could result in substantial imprisonment and a substantial fine in California). So Textron was forced to call these issues to the attention of the Court of Appeal. App. 35. This Court has previously acknowledged that one reason insurance fraud can justify a substantial punitive damages award is because it is a serious wrong that can result in imprisonment. *Pacific Mutual Life Ins. Co. v. Haslip*, 499 U.S. 1, 23 (1991).

The other *BMW* guideposts also suggested that National Union had adequate notice that it could be required to pay a large punitive damages award if it was caught fabricating documents after a loss to fraudulently

and retroactively remove coverage. The ratio of punitive to compensatory damages was 10:1, even based on the actual compensatory award. But when the potential harm is considered, the ratio falls to something much closer to 1:1.

For example, despite the fact that its attorneys spent over 1,500 hours trying to get National Union to honor the claim, the court awarded Textron only $30,000 in legal fees. (*See* PA 13a.) Had the court allowed the jury to award damages based on a reasonable hourly rate (or if Textron had hired its counsel on an hourly basis), the compensatory damages award would have approached or exceeded $500,000.

One of the reasons National Union engaged in the fraudulent scheme to retroactively revoke coverage is that National Union officials feared that the Textron-financed bus might have been carrying passengers at the time of the accident. National Union was concerned that it would have to pay personal injury claims to a large number of injured passengers.

When these harms and potential harms are considered, the ratio becomes quite small in comparison to other punitive damages awards that have been approved by this Court and courts around the country.

Finally, National Union complains that the Court of Appeal did not expressly say that National Union's conduct was extremely reprehensible. This unusual argument is hard to understand. During trial, National Union's own attorney told the jury that if it concluded that National Union had in fact fabricated documents in order to retroactively remove coverage, that would be a vile act. App. 26.

It would be inappropriate for any business entity to falsify documents in order to perpetrate a fraud, and then

secrete and destroy other documents to try to conceal that fraud. But when that conduct is performed by an insurance company – a company that promises security and has a legal duty to act with utmost good faith toward its policyholders – there is simply no room to argue that this is a form of mild conduct that does not warrant the strong medicine of substantial punitive damages.

In this regard, it is worth recalling that *BMW* specifically says "the federal excessiveness inquiry appropriately begins with an identification of the state interests that a punitive award is designed to serve." 517 U.S. at 568. Although National Union has never addressed the state interest component of *BMW*, California has a compelling state interest in being able to deter state-licensed insurers from engaging in fraud as a means of unfairly and improperly denying insurance claims. The United States Congress has specifically declared that state regulation of the business of insurance "is in the public interest. . . . " 15 U.S.C. § 1011. And the California Supreme Court has repeatedly acknowledged the state's strong interest in promoting fair and efficient handling of insurance claims on the part of insurers. *See, e.g., Egan v. Mutual of Omaha Ins. Co.*, 24 Cal.3d 809, 819-820 [620 P.2d 141, 145-146, 169 Cal.Rptr. 691, 695-696] (1979). *See also Foley v. Interactive Data Corp.*, 47 Cal.3d 654, 683-685 [765 P.2d 373, 389-391, 254 Cal.Rptr. 211, 227-229] (1988).

In fact, California law requires policyholders to report punitive damages awards to a state agency in order to help the state police insurers who engage in malicious conduct toward policyholders. Cal. Civ. Code § 3296. California's interest in deterring state-licensed insurers from perpetrating frauds in order to wrongfully deny insurance claims is a significant interest that warranted substantial punitive damages.

Whatever the standard of review, a $1.7 million punitive damages award does not violate the federal constitution when it is imposed against an insurance company that committed an affirmative, deliberate fraud, retroactively removing coverage by fabricating documents.

5. IF THERE WAS NO INDEPENDENT REVIEW, REINSTATEMENT OF THE JURY'S $10 MILLION DAMAGES VERDICT IS APPROPRIATE

National Union successfully urged the trial judge to reduce the jury's $10 million punitive damages verdict on the basis of *BMW*. As explained previously, the trial judge used federal constitutional law to reduce the punitive damages award even though the trial judge determined that National Union had ample notice that its egregious conduct could support a large punitive damages award, and even though National Union had never argued that it lacked adequate notice of the size of the award a jury might render.

In fact, this case included one very unusual feature not found in most punitive damage cases. That is, National Union's own designated claims handling expert told the jury about other cases where National Union had been subjected to punitive damages verdicts. In those cases, the awards were far larger: $43 million and $14 million. App. 28. One of those cases even involved an effort by National Union to retroactively reduce coverage.

National Union cannot seriously argue that it lacked adequate notice that efforts to retroactively remove coverage by creating fabricated fraudulent documents could subject it to a $10 million punitive damages award. Likewise, National Union has never argued that the State of California lacks a strong state interest in preserving the integrity of the insurance claims process and deterring

insurance company fraud, an interest that justified and required significant punitive damages.

Instead, National Union took *BMW*'s three guideposts and tried to divorce them from the end-point of the analysis. In this way, National Union avoided the key determination *BMW* requires: whether the defendant has *fair notice* that its conduct could result in a substantial punitive damages award.

To the extent that another level of independent review of federal punitive damages law is required, it would seem that reinstatement of the jury's $10 million verdict is appropriate.

This is because National Union's post-accident falsification and fabrication of documents (followed by a cover-up) involves the kind of egregious reprehensible conduct that this Court evaluated in *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443 (1993). This case did not involve the kind of generally lawful conduct that was at issue in *BMW* or *Cooper*.

In *TXO*, this Court determined that a $10 million punitive damages award was constitutional even though the defendant's conduct had only caused $19,000 in actual damages. Although the Court acknowledged that the punitive damages award was 526 times as large as the actual damages award, the *TXO* Court found the jury's verdict to be constitutionally valid for the following reasons:

1. The award was based on conduct constituting "bad faith" and affirmative "fraud, trickery and deceit." (509 U.S. at 462);
2. When the potential harm was considered along with the amount of money TXO felt it might be saving itself by engaging in affirmative fraud, the ratio dropped substantially (*id.* at 460-62); and
3. In view of TXO's $2.2-$2.5 billion wealth, strong medicine was required (*id.* at 450, n. 9 and 462).

Just as in *TXO*, National Union's conduct involved affirmative and deliberate deceit. Fraud was then compounded by efforts to conceal the wrongdoing. The ratio between punitive and compensatory damages was actually much *lower* in this case than it was in *TXO*. And both cases involved a defendant whose fraud was in part motivated by a desire to save itself substantial sums of money. Finally, TXO was certainly wealthy, but not nearly as wealthy as National Union.

Beyond *TXO*, this case included evidence that other punitive awards had failed to deter National Union. And in contrast to the arms-length transaction addressed in *TXO*, National Union was a state-licensed insurer that was obligated to treat policyholders with utmost good faith and fair dealing.

Ultimately, even if the Court of Appeal here failed to independently evaluate federal law issues, the only difference a new, independent review could make is the possible reinstatement of jury's $10 million punitive damages verdict. After all, the trial court reduced the punitive damages despite finding that National Union had never even argued that it lacked fair notice that efforts to fabricate fraudulent documents in order to retroactively remove coverage could result in a $10 million punitive damages award. And *BMW* itself distinguishes cases involving affirmative fraudulent wrongdoing. In explaining why it was reversing the punitive damages award in *BMW*, this Court said "the record in this case discloses no deliberate false statements, acts of affirmative misconduct, or concealment of evidence of improper motive, such as were present in *Haslip* and *TXO*." *BMW*, 517 U.S. at 579.

This case involved deliberate, affirmative fraud by an insurance company that was duty-bound to act with utmost

good faith and fair dealing. The $1.7 million punitive damages award was not constitutionally invalid, and neither was the jury's $10 million punitive damages verdict.

CONCLUSION

National Union's petition should be denied. National Union waived the one argument advanced in its petition. And National Union invited the alleged "error" that it is complaining about now.

The California Court of Appeal independently assessed federal law punitive damages principles. And the California Court of Appeal was aware of the fact that those federal standards differ from state law standards.

Even if the California Court of Appeal had not independently assessed federal issues pertaining to punitive damages, the already substantially reduced $1.7 million punitive damages award would be constitutionally valid, regardless of the applicable standard of review. And finally, because this case involved affirmative, deliberate fraud, the jury's $10 million punitive damages award was within the constitutionally valid range prescribed by *TXO*.

National Union's petition should be denied. To the extent this Court believes that yet another level of independent review is required, it should return the case with instructions to reinstate the jury's $10 million punitive damages verdict.

Respectfully submitted,

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G020323

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT
DIVISION THREE

TEXTRON FINANCIAL CORPORATION, a Delaware Corporation,

Plaintiff and Respondent,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Defendant and Appellant.

APPEAL FROM THE SUPERIOR COURT FOR ORANGE COUNTY
RAYMOND J. IKOLA, JUDGE (CASE NO. 734096)

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IV. THE $1.7 MILLION PUNITIVE AWARD VIOLATES NATIONAL UNION'S RIGHT TO DUE PROCESS UNDER THE FOURTEENTH AMENDMENT TO THE UNITED STATES CONSTITUTION AND IS EXCESSIVE UNDER CALIFORNIA LAW.

In Honda Motor Co., Ltd. v. Oberg (1994) 512 U.S. 415 [129 L.Ed.2d 336, 114 S.Ct. 2331], the United States Supreme Court, recognizing that "punitive damages pose an acute danger of arbitrary deprivation of property," held that judicial review of the size of a punitive damage award is mandated by the due process clause of the United States Constitution. (*Id.* at p. ___ [114 S.Ct. at p. 2340]; see also *Adams v. Murakami* (1991) 54 Cal.3d 105, 118 [recognizing a "constitutional mandate for meaningful judicial scrutiny of punitive damages awards"]; *Las Palmas Associates v. Las Palmas Center Associates* (1991) 235 Cal.App.3d 1220, 1258 ["Appellate courts must scrutinize punitive damage verdicts because they 'constitute a windfall, create the anomaly of excessive compensation, and are therefore not favored in the law' "].)

No punitive damages are warranted in this case. Even if they are, the $1.7 million award is excessive.

In *BMW of North America, Inc. v. Gore, supra,* ___ U.S. ___ [134 L.Ed.2d 809, 116 S.Ct. 1589], the United States Supreme Court identified three "guideposts" for evaluating whether punitive damage awards are constitutionally excessive: "degree of reprehensibility" (*id.* at p. ___ [116 S.Ct. at p. 1599); "ratio [of punitive damages] to the actual harm inflicted on the plaintiff" (*id.* at p. 1601); and

"civil or criminal penalties that could be imposed for comparable misconduct" (*id.* at p. 1603). Following *BMW*, the courts nationwide have applied its three guideposts to reverse or substantially reduce punitive damage awards. (See, e.g., *Management Computer Services, Inc. v. Hawkins, Ash, Baptie & Co.* (1996) 206 Wis.2d 157, ___ [557 N.W.2d 67, 82] [$1.75 million award reduced to $650,000 because defendant's conduct, although "both grievous and malicious," caused only economic injury].) In *BMW* itself, the Alabama Supreme Court on remand held that punitive damages awarded because the defendant "suppressed a material fact" could not exceed $50,000, even though previously it had held $2,000,000 was appropriate. (*BMW of North America, Inc. v. Gore,* 1997 Ala. LEXIS 126.)

As we have shown, the jury probably awarded punitive damages on account of TRM's conduct, not the conduct of the AIAC adjustors. (*Ante,* § I.E.) But, regardless of the basis for the award, when examined in light of the three *BMW* guideposts, it violates National Union's right to due process under the Fourteenth Amendment. It is also excessive under California law.

First, *BMW* held that "the degree of reprehensibility of the defendant's conduct" is "[p]erhaps the most important indicium of the reasonableness of a punitive damage award." (*BMW of North America, Inc. v. Gore, supra,* ___ U.S. at p. ___ [116 S.Ct. at p. 1599].) Even if TRM was National Union's managing agent and National Union therefore is technically responsible for its conduct, National Union's own behavior does not involve "the high degree of culpability that warrants a substantial punitive damages award." (*Id.* at p. 1601.) If TRM

engaged in post-accident underwriting, its conduct was reprehensible. But National Union's liability for that conduct is derivative, not direct. It cannot discipline TRM because TRM is not National Union's employee and a large award is unnecessary to deter National Union from further dealings with TRM – it ceased doing business with TRM in January of 1995. Indeed, Textron settled with TRM for only $62,500. What possible justification can there be for letting the actual wrongdoer off the hook for $62,500 while socking its principal, who at most was derivatively liable, with a $1.7 million penalty?

If the jury's punitive damage award was based on the conduct of AIAC's adjusters, the excessiveness of a $1.7 million punitive award is even clearer. At most, the adjusters denied a single property damage claim based on a misreading of the insurance policy. Just as in *BMW*,

> "none of the aggravating factors associated with particularly reprehensible conduct is present. The harm . . . was purely economic in nature . . . . [National Union's] conduct evinced no indifference to or reckless disregard for the health and safety of others. To be sure, infliction of economic injury, especially when done intentionally through affirmative acts of misconduct, . . . or when the target is financially vulnerable, can warrant a substantial penalty. *But this observation does not convert all acts that cause economic harm into torts that are sufficiently reprehensible to justify a significant sanction in addition to compensatory damages.*"

(*BMW of North America, Inc. v. Gore, supra,* ___ U.S. at p. ___ [116 S.Ct. at p. 1599], emphasis added.)

Unlike the typical plaintiff in an insurance bad faith action, Textron was not "financially vulnerable." (*Ibid.*) It is a "sophisticated" entity "with the financial resources to weather . . . sharp business practices." (*Las Palmas Associates v. Las Palmas Center Associates, supra,* 235 Cal.App.3d at p. 1255.) Like the insured in *Slottow v. American Cas. Co.* (9th Cir. 1993) 10 F.3d 1355, where the court disallowed any punitive damages in a suit by a bank against an insurance company, Textron has "ready access to legal advice and controls substantial assets, placing it on relatively equal footing with [National Union]." (*Id.* at p. 1362.) Just as in *Slottow,* neither Textron nor National Union "faced a threat to its existence or financial stability because of this dispute; each simply went about its business while the controversy percolated." (*Ibid.;* see also *Seeley v. Seymour* (1987) 190 Cal.App.3d 844, 867 ["the parties here were sophisticated businessmen of relatively equal bargaining strength. The situation at bar thus carries a lesser degree of 'reprehensibility' than the more typical punitive damage case where a large or sophisticated business enterprise uses its wealth or power to exploit the weak or the unwary"].)

Moreover, *BMW* recognized that "repeated misconduct is more reprehensible than an individual instance of malfeasance." (*BMW of North America, Inc. v. Gore, supra,* ___ U.S. at p. ___ [116 S.Ct. at pp. 1599, 1600].) Here, as we have shown, there was no evidence that National Union had ever previously received, let alone denied, a claim by a loss payee who did not receive advance notice of a cancellation or deletion. (RT. pp. 2223-2224, 4858.)

Second, $1.7 million in punitive damages cannot be justified by the ratio of punitive damages to the actual

harm inflicted on Textron. In *Pacific Mut. Life Ins. Co. v. Haslip* (1991) 499 U.S. 1 [113 L.Ed.2d 1, 111 S.Ct. 1032], the United States Supreme Court explained that a ratio of 4.2 to I between punitive and compensatory damages is "close to the line" of constitutional impropriety. (*Id.* at pp. 23-24.) In *Cates Construction, Inc. v. Talbot Partners* (1997) 53 Cal.App.4th 1420, the most recent pronouncement on punitive damages by a California appellate court, the court, citing *BMW*, held that "a ratio in the order of nine to one . . . can be said to be 'close to the line' of federal constitutional impropriety" and accordingly reduced the punitive award to five times the actual economic harm caused by the insurer's bad faith conduct. (*Id.* at p. 1460.)[35] Here, The $1.7 million award is approximately 96 times Textron's actual loss, $17,683.60. (See *ante*, § III.) Although the award is approximately 10 times the $165,000 compensatory damage award, the latter figure overvalues Textron's true loss because the trial court erroneously allocated the $89,000 in pretrial settlements to nonduplicative damages. (*Ante*, § II.) Moreover, even

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[35] In *TXO Production Corp. v. Alliance Resources Corp.* (1993) ___ U.S. ___ [125 L.Ed.2d 366, 113 S.Ct. 2711], the United States Supreme Court upheld against a due process challenge to a ratio of not more than 10 to 1 between compensatory and punitive damages. There the punitive award was $10 million and the harm to the victim that would have ensued if the tortious plan had succeeded was at least $1 million. Moreover, the United States Supreme Court noted that the defendant had a history of "nefarious activities in its business dealings" (*id.* at p. ___ [113 S.Ct. at pp. 2716-2717]) and the punitive award was intended to punish not just the defendant's conduct in that case, but its general manner of doing business. (*Id.* at p. ___ [113 S.Ct. at pp. 2722-2723].)

without an offset, the ratio between the punitive award and the tort damages (*Brandt* fees) is over 19 to 1. As *Haslip* and *Cates* demonstrate, whether the ratio in this case is 96 to 1, 19 to 1 or 10 to 1, it crosses the line of constitutional impropriety.[36]

Ratios between compensatory and punitive damages considerably lower than 96 to 1 or even 10 to 1 have also been held excessive under California law. (See e.g., *Little v. Stuyvesant Life Ins. Co.* (1977) 67 Cal.App.3d 451, 469-470 [reversal of punitive award 14 times greater than compensatory damages unless remittitur to amount 1.5 times greater accepted]; *Allard v. Church of Scientology* (1976) 58 Cal.App.3d 439 [reversal of punitive award 5 times greater than compensatory damages unless remittitur to amount in 1 to 1 ratio accepted].) In the insurance context, ratios 10 to 1 or greater have generally been upheld only where the compensatory award was significantly under $100,000 (see, e.g., *Moore v. American United*

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[36] In determining whether the punitive award is excessive, the proper comparison is between that award and the tort damages, not the combined contract and tort award. This is so because "[an] award of punitive damages is not supported by a verdict based on breach of contract. . . . " (*Myers Building Industries, Ltd. v. Interface Technology, Inc.* (1993) 13 Cal.App.4th 949, 960; accord *Crogan v. Metz* (1956) 47 Cal.2d 398, 405; see Civ. Code, § 3294, subd. (a).) Because the contract damages were not awarded as compensation for tortious breach of the covenant of good faith and fair dealing, they cannot support the punitive award. Indeed, Textron was entitled to *Brandt* fees only for recovering policy benefits, i.e., contract damages. (*Brandt v. Superior Court, supra,* 37 Cal.3d 813.) Textron cannot treat policy benefits as contract damages for purposes of awarding *Brandt* fees and at the same time treat them as tort damages for purposes of calculating a punitive damage award.

Life Insurance Co. (1984) 150 Cal.App.3d 610; *Pistorius v. Prudential Ins. Co.* (1981) 123 Cal.App.3d 541; *Neal v. Farmers Ins. Exchange* (1978) 21 Cal.3d 910; *Wetherbee v. United Ins. Co. of America* (1971) 18 Cal.App.3d 266) and/or in cases involving especially egregious or widespread company practices. (See, e.g., *Moore v. American United Life Ins. Co., supra,* 150 Cal.App.3d 610; *Downey Savings & Loan Assn. v. Ohio Casualty Ins. Co.* (1987) 189 Cal.App.3d 1072.) Even these cases, of course, predate the United States Supreme Court's decision in *BMW.*

Third, turning to the civil or criminal penalties that could be imposed for comparable misconduct, the maximum statutory penalty established for insurance bad faith is $10,000. (Ins. Code, § 790.035.) Even a willful violation of a cease and desist order risks a maximum penalty of merely $55,000. (Ins. Code, § 790.07.) The Legislature evidently concluded a million dollar award is unnecessary to sufficiently punish and deter such bad faith conduct.

Finally, although National Union has substantial assets, ability to pay, in and of itself, cannot be used to justify a "multimillion dollar award." (*Adams v. Murakami, supra,* 54 Cal.3d at p. 111, fn.2.) As the United States Supreme Court explained in *BMW:*

> "The fact that a multimillion dollar penalty prompted a change in policy sheds no light on the question whether a lesser deterrent would have adequately protected the interests of Alabama consumers. In the absence of a history of noncompliance with known statutory requirements, there is no basis for assuming that a

> more modest sanction would not have been sufficient to motivate full compliance. . . . " (*BMW of North America, Inc. v. Gore, supra,* ___ U.S. at p. ___ [116 S.Ct at p. 1603].)

In short, the United States Supreme Court focuses on the *least* amount that will deter, not on *any* amount that will deter that the defendant can afford. Here, *no* punitive damages are necessary for deterrence. National Union ceased doing business with TRM, the actual wrongdoer, long before this case came to trial, and modified its own procedures regarding notices to loss payees before the jury announced its punitive damage award. (R.T. pp. 4857-4858.) If any penalty is necessary to deter future misconduct, that penalty is substantially less than $1.7 million.

* * *

4th Civil No. G020323

IN THE COURT OF APPEAL OF THE
STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORPORATION,

Plaintiff, Respondent, Cross-Appellant (and Separate Appellant),

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al.

Defendants and Appellants.

On Appeal From The Superior Court of
Orange County
Hon. Raymond J. Ikola
Case No. 734096

TEXTRON'S OPENING BRIEF ON ITS CROSS-APPEAL

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3. The Decisions Relied on By The Trial Court Were Not Apt Or Controlling.

In it's reduction of punitive damages, the court relied primarily on two cases – *BMW of North America, Inc. v. Gore* (1996) 116 S.Ct. 1589 and *Rosener v. Sears, Roebuck & Co.* (1980) 110 Cal.App.3d 740. (C.T. 4826.) From the comparison of the punitive damages figure to the compensatory damages award, the trial court concluded that the 60:1 ratio created a "presumption" that the jury acted from passion or prejudice. (C.T. 4826.) In this analysis, the court's reliance on *BMW* and *Rosener* was misplaced.

In *BMW*, a $2 million punitive damages judgment was assessed against *BMW* because it did not disclose that it had made $600 in paint repairs to a car it sold. The Alabama Deceptive Practices Act authorized a $2,000 civil penalty for BMW's alleged conduct. 116 S.Ct. at 1603. However, BMW's conduct was perfectly legal in most states. *Id.* at 1596, fn. 13.

There are several reasons *BMW* is inapplicable to this case. Perhaps most significantly, *BMW* expressly distinguished cases involving deliberate false statements or other affirmative misconduct. As the *BMW* court explained, "the record in this case discloses no deliberate false statements, acts of affirmative misconduct, or concealment of evidence of improper motive, such as were present in *Haslip* and *TXO*." *Id.*, at 1601. In sharp contrast to *BMW*, this case included substantial clear and convincing evidence of egregious affirmative misconduct, including the post-claim alteration of an insurance policy, concealment and destruction of evidence, and sustained efforts to conceal the misconduct. When it expressly distinguished *TXO*, the *BMW* court necessarily distinguished the case at bench.

In addition, *BMW* emphasized that any assessment of punitive damages must start with an evaluation of the state's interest the award is designed to serve. Only when "an award can fairly be categorized as 'grossly excessive' *in relation to these interests*" does it violate due process. *Id.* Different classes of cases require differing assessments. *Id.* at 1595. (emphasis added). This case and *BMW* are in different classes.

California's interest in deterring state-licensed insurance businesses from fraudulent, bad faith claims practices is significantly greater, and far more urgent, than Alabama's interest in deterring non-disclosure of $600 paint repairs on luxury cars.[5] California even uses punitive damages to help it police insurance companies. It affirmatively requires policyholders such as Textron to report punitive damage verdicts to the Insurance Commissioner. Civ. Code § 3296.

Finally, the trial court analyzed *BMW*'s "three guideposts" without placing them in proper context. These guideposts are (1) reprehensibility of the conduct; (2) disparity between harm or potential harm and the punitive damages award; and (3) the amount of civil penalties authorized or imposed in other cases. Reprehensibility is the most important. 116 S.Ct. at 1598.

BMW held that in some circumstances an award of punitive damages that is "grossly excessive" can violate due process of law because a person is entitled to "fair notice not only of the conduct that will subject him to punishment but also of the severity of the penalty that a State may impose." *Id.* at 1598.

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[5] California courts have often noted that insurance contracts are different than ordinary commercial contracts. Insurance policies serve a quasi-public purpose. There is a "special relationship" between the insurer and the insured. And, unlike the vast majority of contracts, insurance policies are not purchased to secure commercial advantage, but to protect against calamity. See, e.g., *Foley v. Interactive Data Corp.* (1988) 47 Cal.3d 654, 684-85.

But, the trial court reduced the jury's verdict despite concluding that National Union did indeed have fair notice that its misconduct could result in imposition of substantial punitive damages. As the court explained:

> "Surely National Union does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law." (C.T. 4828.)

The other case the trial court emphasized in reducing the jury's verdict was *Rosener v. Sears, Roebuck & Co* (1980) 110 Cal.App.3d 740. With the exception of some mathematical similarities, *Rosener* bears no relationship to this case. In *Rosener*, liability was based largely on the *negligence* of Sears in completing construction contracts after one of its contractors had financial problems. *Id.* at 747. Unlike the present case, *Rosener* involved no deliberate misconduct, no affirmative misrepresentations, no fabricated documents, and no destruction of evidence. In addition, there was no evidence that earlier punitive damage awards had failed to deter the defendant's conduct.

In addition, one of the issues in *Rosener* was that the jury was not instructed on the requirement that the punitive damages bear a reasonable relationship to the harm. *Id.* at 753. In contrast, the jury in the present case received such instruction. (C.T. 3837.)

Rosener also was the kind of case that is more likely to generate jury passion or prejudice – a "little guy" up against a big company. *Id.* at 747. As the United States Supreme Court explained in *Honda Motor Co. v. Oberg*

(1994) 512 U.S. 415, 114 S.Ct. 2331, 129 L.Ed.2d 336, the basic reason for post-trial review of punitive damage awards is that juries may be tempted to "use their verdicts to express biases against big businesses, particularly those without strong local presences." 512 U.S. at 432. That possibility was not present in this case. In complete contrast to *Rosener*, both parties in this case were big businesses, and National Union repeatedly reminded the jury of that fact.

Rosener's mathematical similarity to this case is not controlling. Instead, courts invariably rule that a mathematical formula is *not* an appropriate way to review a punitive damages verdict. See, e.g., *Devlin v. Kearney Mesa AMC/Jeep/Renault, Inc.* (1984) 155 Cal.App.3d 381, 390 (The "calculation of punitive damages does not involve strict adherence to a rigid formula."); *Adams v. Murakami* (1991) 54 Cal.3d 105, 112 ("The determination of whether an award is excessive is admittedly more art than science."); *Pacific Mut. Life Ins. Co. v. Haslip*, (1991) 499 U.S. 1, 18 ("We cannot . . . draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable.").

While the trial court misapplied *BMW* and *Rosener*, it did not apply other cases that involved factual scenarios more like this case. For example, in *TXO, supra*, the United States Supreme Court upheld a jury's $10 million punitive damages verdict in a case involving only $19,000 in actual damages, a ratio of 526:1. (509 U.S. at 446-47.)

Much as National Union did in this case, TXO apparently tried to fabricate false documents (*Id.* at 449), and engaged in fraud, trickery and deceit. *Id.* at 453. When a

case involves fabrication of documents and concealment and destruction of evidence, as this case did, a $10 million punitive damages verdict is very appropriate. This is especially true since National Union conducts its business under a license granted by the State of California, and because it's net worth ($3.7 billion) was half again as large as the net worth of TXO ($2.5 billion). *TXO*, 509 U.S. 443, 451, fn. 9.

By isolating the mechanical application of a mathematical formula involving the ratio of punitive to compensatory damages, the trial court failed to give full consideration to the factors identified in *BMW, TXO* and other cases. For example, in *Downey Savings & Loan Assoc. v. Ohio Cas. Ins. Co.* (1987) 189 Cal.App.3d 1072, 1097, the court upheld a $5 million punitive damages award on compensatory damages of $152,000 – a 32.7:1 ratio. The *Downey Savings* court noted the obvious. Unlike plaintiffs in many punitive damages cases, the plaintiff in *Downey Savings* was a large corporation (like Textron). It was *not* a plaintiff likely to arouse the jury's passion, prejudice, or even sympathy. *Id.* at 1099.

This case is much like *Downey Savings*. The jury that decided this case was repeatedly told that Textron was a big company. National Union told the jury that this case was between "two big boys," and (falsely) that Textron was larger than AIG. (R.T. 4891.) Even National Union's retained claim handling expert took time to remind the jury that Textron was a "multi-billion dollar entity." (R.T. 3847.) The jury was told that the case involved two large corporations, both of whom are headquartered out of state. (R.T. 939, 1653.) The jury was even told that it was Textron who was picking on the "little guy." (R.T. 562.)

National Union went so far as to tell the jury that it was Textron, rather than National Union, who drove Mr. Ko into bankruptcy. (R.T. 563.)[6]

Another important factor deserved consideration. In *TXQ*, the court held that "possible harm to other victims that might have resulted if similar future-behavior were not deterred" is an appropriate consideration. 509 U.S. at 460. As an insurer willing to commit blatant after-the-fact fraud to deny claims, National Union poses a serious threat not just to Textron, Ko, and CNA – the parties it injured in this particular instance – but to all California

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[6] Ironically enough, if anyone appealed to passion and prejudice, it was National Union. With theatrics right out of a bad episode of "Perry Mason," National Union actually had one witness set her watch alarm while testifying. When the alarm sounded, the witness casually told the jury she had to "get to church on time." (R.T. 3050.)

National Union's counsel often tried to divert attention away from the facts and toward emotions. For example, National Union's counsel took time to ask Rochelle Ware about the "fact" that she went back to her office to catch up on her work during court recesses. (R.T. 2496.) The jury was even told about Ms. Ware's child care responsibilities. (R.T. 2497-98.)

During closing arguments in Phase II, National Union's counsel asked the jury to focus on the local claims people who became involved with the file (Rochelle Ware, Ella Quinlan and Tom Lyons), rather than National Union's Home Office personnel such as Division 20 Director, Larry Kelly, John Lavin or Don Schmitz, and TRM's president, Tom Spangenberg. National Union told the jury it wouldn't find a "sweeter, kinder person than Rochelle Ware." And National Union told the jury that a "bad-faith finding would be with them all their lives." (R.T. 4656-57.) So if passion or prejudice played any part in the jury's punitive damages verdict, it most likely reduced the verdict.

residents unlucky enough to be involved in a claim where AIG has issued the coverage.

In addition to the insufficient *Brandt* fee award mentioned previously, there was also the potential for more economic harm in this case. Had passengers been on the bus when the accident occurred, National Union's fraudulent "deletion" endorsement would have been asserted to avoid payment of the policy's $5 million in liability insurance, plus defense costs.[7]

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[7] National Union's policy included $5 million in liability insurance. (Ex. 198, p. 38.) All certificate holders were additional insureds for liabilities arising out of the operations of the named insured. (Ex. 198, p. 45.) Textron was a certificate holder. (Ex. 4.) So its liability insurance protection was $5 million. If the accident had occurred *after* the bus had picked up the stranded passengers, people would have been hurt and Textron (or Ko) may have needed every penny of the $5 million liability limits. The evidence suggested that part of National Union's motive for trying to retroactively remove coverage may have emanated from a concern that the accident included personal injury liabilities, perhaps sufficient to threaten the National Union/TRM bus program itself. For example, Longuil's "memo for the record" mentioned that he "would not be surprised that we receive a personal injury claim on this one." (Ex. 30.) And Longuil mentioned the concern that if coverage was afforded "it could possibly jeopardize [our] program." (Ex. 80, p. 6.)

Mr. Longuil had also pointed out that because the Public Utilities Commission had obviously not been notified of any purported decision, any liability claim, including the claim made by CNA (the company who insured the truck that was hit by the Textron bus), would have to be paid. (Ex. 30.) Nevertheless, National Union denied both the collision and the liability claims on February 24, 1993. (Ex. 43.) National Union did not call Longuil as a witness at trial.

National Union knew there was coverage for this accident, but it found out it was dealing with some unsophisticated claimants – an insured who didn't speak English and a broker who really didn't know the details of lay-up credits (the particular underwriting practice involved). So National Union took advantage of their relative ignorance and denied the claims. When Textron started asking questions, a "deletion" endorsement was fabricated, and other damaging evidence was removed, withheld, and ultimately destroyed.

Punitive damage awards must be large enough to deter the defendant (and others) from similar future misconduct. *Adams v. Murakami* (1991) 54 Cal.3d 105, 110 (the purpose of punitive damages "is to punish wrongdoing" and protect against "future misconduct, either by the same defendant or other potential wrongdoers."). See also *TXO, supra,* 509 U.S. at 460-461. It is difficult to imagine how a $1.7 million award can affect a company that makes a *net profit* of $850,000 a day, seven days a week, 365 days a year. (R.T. 4902; Ex. 240.)

During the trial of this case (46 days), National Union generated *net* profits of over $39,000,000 – almost four times the jury's $10 million verdict – 23 times more than the trial court's $1.7 million remittitur. National Union had already made its $1.7 million back before the third day of trial even started. Perhaps that is why AIG routinely tells shareholders in its annual report that while it is commonly subjected to punitive damages claims, it "does not believe that such litigation will have a material effect on its operating results and financial condition." (C.T. 4775.)

Finally, the trial court failed to consider the fact that isolating attention on the ratio of punitive damages to compensatory damages actually rewards and encourages conduct such as National Union's. As Textron explained in its opposition to National Union's motion for new trial, one reason National Union resisted Textron so fiercely was that it knew the claim was relatively small. (C.T. 4285.) It knew it could make Textron spend a lot more than the $65,000 before Textron would ever recover a penny. So National Union believed that if it could hold out long enough, Textron would decide to drop the matter.

The fact that a malicious defendant can take particular advantage of a situation involving a relatively small claim may be particularly likely in the insurance context. It is certainly one significant reason courts have held that the ratio between punitive and compensatory damages is less important when the compensatory damages are relatively small. See, e.g., *Downey Savings*, 189 Cal.App.3d at 1098 ("In that situation, a large award of punitive damages would be necessary to ensure that the defendant does not repeat his act and that others do not follow his example.").

The trial court's exclusive focus on the ratio sends the wrong message to National Union, and other insurers. It encourages them to deny claims arbitrarily when the plaintiffs claim is small, comfortable in the belief that even if the jury finds bad faith and malice, punitive damages will still be limited.

There was nothing to distinguish this case from *TXO* or *Downey Savings*, and the trial court erred in concluding

that the jury's $10 million punitive damages verdict was the result of passion or prejudice. So, even if the trial court made a proper ruling when it decided to limit Textron's attorney fee damages to just a little over $30,000, it still failed to consider the reprehensibility of National Union's behavior, and the other potential harm that could have been suffered by Textron (or others) as a result of that behavior.

4. The Jury's Verdict Was Appropriate Even If The Compensatory Damages Are Not Increased

Even if the trial court's remittitur had not included improper conditions, and even if Textron's *Brandt* fee damages could properly be viewed as being limited to $30,268, the trial court still had no basis for concluding that the jury's $10 million punitive damages verdict was "clearly erroneous." By statute, the trial court was not permitted to conditionally reduce the punitive damages verdict unless the evidence established that the jury's verdict was "*clearly* erroneous." Code Civ. Proc. § 657 (emphasis added). See *Big Boy v. County of San Diego* (1984) 154 Cal.App.3d 397, 405 (A new trial is appropriate only if the record is sufficient to convince "the trial judge the jury *clearly* should have reached a different decision.") (emphasis added).

In this instance, many factors supported the jury's $10 million verdict. First, the reprehensibility of the misconduct fell at the extreme end of the spectrum. As National Union's counsel explained during closing argument, if the jury determined National Union fabricated the "deletion" endorsement after the fact in an effort to

remove coverage retroactively that "would be pretty vile." (R.T. 4642.) That is exactly what the evidence showed and what the jury determined. National Union knowingly fabricated a purported "deletion" endorsement after the bus accident to make it appear there was no coverage.

National Union knew it had implemented a lay-up credit, in fact, and had reinstated the entire policy *before* the accident.

National Union also destroyed and tampered with evidence. For example, as National Union's counsel put it, "some idiot" destroyed the Portland claim file jacket. (R.T. 4645, 2970-71.) The jury knew there was no legitimate reason for National Union to destroy the file jacket. (R.T. 3616.) It was entitled to conclude that National Union destroyed the file jacket during the litigation because it contained information National Union preferred to conceal from the jury.

Letters about the lay-up credit, including references to the "much easier way of doing it," were removed from the underwriting file before it was produced to Textron. (R.T. 1623-24.)

Even when National Union gave Textron a purported "copy" of the "deletion" version of endorsement No. 8, a "mailing certificate" was placed over the creation date before it was sent to Textron. National Union wanted Textron to have the impression the document was created in 1992 (before the January 7, 1993 accident), when in fact it was actually created much later, after the accident. (Exs. 189, 33; R.T. 614-15.)

For seven months, National Union flatly refused to give Textron – its own additional insured and designated loss payee – a copy of the policy. In March of 1994 National Union's Home Office sent AIAC – but not Textron – a copy of the original policy. (R.T. 606-07, 965-72, 2312-13.) The original policy did not include any "deletion" endorsement No. 8; the endorsement No. 8 in the original policy was only a *credit* endorsement. It did not purport to eliminate coverage for the bus. (Ex. 198, p. 67.)

In August of 1994, when it finally gave Textron a policy, National Union created a so-called "certified" policy in which it replaced the original credit endorsement with a "deletion" endorsement. (Ex. 78, p. 42.) National Union did not produce its original Home Office policy (with the credit endorsement) until after the lawsuit was underway and Textron had filed a motion to compel production of documents. (C.T. 148-280.)

And although its fraudulent scheme was clearly exposed, National Union was not, and still is not, the least bit repentant. Except for National Union, every defendant in the case seemed to acknowledge some degree of fault. Ferguson admitted he had not given Textron good service. (R.T. 836.) After moving its program to a different insurance company, TRM acknowledged that suspensions did not remove physical damage coverage. (Ex. 107.) Even AIAC said it would make some changes. (R.T. 4858.)

Only National Union insisted and continues to insist that it did nothing wrong. The head of National Union's Division 20 – the Division that issued this policy – inexplicably testified that the fabricated deletion version of

endorsement No. 8 was a "courtesy" National Union performed for Textron. (R.T. 1739.) And the adjuster who testified that National Union would withhold Textron's claim payment as a means of "litigation posturing" said the same thing. (R.T. 2680.) He said National Union was doing Textron a favor by sending the fabricated "deletion" endorsement after the accident, so Textron wouldn't "get screwed." (R.T. 2650-51.)

No insured should be forced to endure such outrageous behavior. The reprehensibility of the conduct of this state-licensed insurer in its post-claim alteration of the policy, fabrication of documents, and concealment and destruction of evidence, was severe, sustained, and outrageous. This was deliberate insurance fraud.[8]

Next, unlike most (or perhaps all) cases where courts have reduced punitive damages verdicts, in this case, there was evidence of National Union's recidivism. This was not the first time National Union faced imposition of punitive damages for bad faith claims handling. In fact, it was not the first time National Union faced punitive damages for trying to retroactively terminate coverage in order to avoid paying claims. (R.T. 158.) Claims handling experts for both Textron and National Union testified about larger punitive damage verdicts against National Union – $43 million and $14 million – but those verdicts

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[8] If a policyholder got caught perpetrating such a fraud, he could wind up in prison for several years. See, e.g., Pen. Code § 550 (providing penalties of up to five (5) years imprisonment, plus fines, for knowingly making false or misleading statements in support of (or in opposition to) a claim for insurance benefits).

didn't stop it from committing fraud to support its unjust and manufactured denials of the claims here. (R.T. 3451-53; 3511, 3517-18; 3808-11.)

The testimony of Textron's expert was supported by National Union's own claims handling expert, James Roberts. Mr. Roberts agreed that National Union makes bad faith claims handling a practice. (R.T. 3830-31.) He explained that National Union routinely "lies to all of its policyholders about being open-minded." (R.T. 3828-30.)

In addition, the jury knew it would take a significant award just to get National Union's attention. Robert Thomas was designated as National Union's most knowledgeable person concerning claims handling. Despite the fact that the claims addressed in *Helfand v. National Union Fire Ins.* Co. (1992) 10 Cal.App.4th 869, 879, resulted in a "judgment against National Union" that included "$43 million in punitive damages," Mr. Thomas testified that he had never even heard of *Helfand*. (Ex. 237, p. 47.)[9]

Ms. Quinlan, a claim manager actively involved with Textron's claim, testified that she had to read about the *Helfand* decision in the newspapers because it was not discussed internally at AIG. (R.T. 2992-95.)

This kind of evidence permitted the jury to conclude either that National Union had no training procedures to

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[9] In *Helfand* the appellate court upheld the finding of bad faith based on National Unions efforts to avoid payment by canceling coverage after it discovered "Big Problems," but the punitive damages verdict was reversed because of other, unrelated errors. 10 Cal.App.4th at 878, 904. Textron understands the case was subsequently settled on confidential terms.

help guard against future malicious misconduct against policyholders, or worse, that National Union made a conscious effort to keep its employees ignorant of substantial verdicts against National Union. As Textron's expert testified, open discussion of company misconduct in other cases is critical for proper training of claims handlers. (R.T. 3453.)

The jury was also aware that despite such egregious misconduct, no one at National Union was ever criticized for his or her work on the Textron claim. In fact, during the trial, employees boasted they were proud of the way National Union handled the claim. (R.T. 3235.)

Textron's expert testified that the lack of criticism of employees showed not only that National Union endorsed and ratified the conduct, but that National Union had a corporate culture that tolerated (or even condoned or rewarded) bad faith conduct against policyholders. (R.T. 3494-96.) The jury certainly was entitled to conclude that the corporate culture at National Union involves "an unwillingness and inability, apparently, to simply fess up to a problem and address it." (R.T. 3494.) One employee testified that it is company policy *not* to acknowledge mistakes. (R.T. 2950.)

No trial court could have rationally concluded that this jury's punitive damages verdict was *clearly* the result of passion or prejudice or that $1.7 million would have the necessary deterrent effect.

* * *

4th Civil No. G020323

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORPORATION,

Plaintiff, Respondent, Cross-Appellant (and Separate Appellant),

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al.

Defendants and Appellants.

On Appeal From The Superior Court of Orange County
Hon. Raymond J. Ikola
Case No. 734096

TEXTRON'S RESPONDENT'S BRIEF

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* * *

G. THE PUNITIVE DAMAGES AWARD WAS NOT EXCESSIVE

In section 3.B. of its cross-appeal, Textron explains why the jury's $10 million dollar punitive damages verdict was appropriate, and indeed, should be reinstated. Of necessity, therefore, those same points establish that

the award of $1.7 [sic] ultimately granted by the trial court was excessive. Rather than repeat arguments, Textron simply incorporates by this reference section 3.B. of its Opening Brief on its Cross-Appeal as if set forth in full. (pp. 8-26.)

To argue against punitive damages, National Union assumes that it did nothing wrong, and only TRM engaged in wrongdoing. But Textron has already demonstrated National Union's involvement in denying the claim and ratifying TRM's actions.

National Union's reliance on *Slottow v. American Cas. Co.* (9th Cir. 1993) 10 F.3d 1355, is erroneous. *Slottow* did not hold that insurance companies are free to commit fraud against corporate policyholders, secure in the knowledge that they are immune from punitive damages. In *Slottow*, the record did not support any "finding that the insurance company acted fraudulently." *Id.* at 1362. Here, by contrast, National Union committed fraud. Likewise, while in *Slottow* there was no "showing that [the insurer] acted with malice" the jury found not just that National Union had acted with malice, but that it also had acted with fraud and oppression.

The fact Textron is a substantial corporation with assets may have indicated to the jury that a significant deterrent was required precisely because if left unchecked, the same tactics National Union used against Textron might put smaller insureds out of business.

National Union's argument it did not have fair notice of the possibility of a multi-million dollar punitive damages award because of the comparable civil and criminal penalties is erroneous for two reasons. The evidence

showed National Union had already been subjected to far larger punitive damages verdicts as a result of its bad faith claims handling, so it had more than adequate notice. In addition, National Union has inaccurately argued the maximum civil or criminal penalty that might be imposed for similar misconduct is $55,000. To the contrary, the maximum criminal penalty for insurance fraud is 5 years imprisonment, *plus* a $50,000 fine. Pen. Code § 550. The maximum civil penalty that can be imposed by the California Insurance Department can include suspension or revocation of a license or certificate – a penalty that would cost National Union far more than the jury's $10 million dollar punitive damages verdict.[43] Ins. Code § 790.07.

* * *

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[43] National Union again argues that for purposes of assessing punitive damages, its misconduct must be divided between damages caused by its breach of contract, and damages caused by its tortious wrongdoing. National Union forgets an insurer's unreasonable breach of contract *is* tortious. (R.T. 4829-36; C.T. 3702-08.)

G020323

IN THE COURT OF APPEAL
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a Delaware Corporation,

Plaintiff and Respondent,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Defendant and Appellant.

APPEAL FROM THE SUPERIOR COURT FOR ORANGE COUNTY
RAYMOND J. IKOLA, JUDGE (CASE NO. 734096)

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INTRODUCTION

The principal issue on this appeal is whether the trial court erred by instructing that TRM was National Union's managing agent under Civil Code section 3294. If the instruction was erroneous, the punitive damage award must be reversed so long as there was "a *reasonable chance,* more than an *abstract possibility*" (*College Hospital Inc. v. Superior Court* (1994) 8 Cal.4th 704, 715) the jury would not have awarded punitive damages absent the error.

* * *

B. The Trial Court Properly Found That The Jury's $10 Million Punitive Damage Award Was Excessive.

Our discussion as to why even the remitted $1.7 million punitive damage award violates National Union's federal due process rights and is excessive under California law (A.O.B. § IV; A.R.B., § VIII) disposes of Textron's contention that the trial court erred in remitting the jury's $10 million punitive damage award. If $1.7 million is too high, *a fortiori* it would be improper to reinstate the jury's $10 million award. Rather than repeat our arguments as to why even the $1.7 million award is excessive, we incorporate those arguments by reference.

Even if $10 million were not excessive as a matter of law, the trial court's remittitur should not be reversed. As the Supreme Court explained in *Neal v. Farmers Ins. Exchange, supra,* 21 Cal.3d 910:

> "[W]hen a trial court grants a new trial on the issue of excessive damages, whether or not such order is conditioned by a demand for reduction, the presumption of correctness normally accorded on appeal to the jury's verdict is replaced by a presumption in favor of the order. . . . 'whatever may be the rule which should govern the trial judge, it is certain that when his action in granting a new trial on the ground of excessive damages, or requiring a reduction of the amount as the condition of denying one, comes to be reviewed on appeal, his order will not be reversed unless it plainly appears that he abused his discretion;. . . . ' . . . The reason for this is that the trial court, in ruling on the motion, sits not in an appellate

capacity but as an independent trier of fact." (*Id.* at pp. 932-933.)

No abuse of discretion occurred here. Textron's attack on the remittitur assumes that National Union actively conspired with TRM to fabricate documents and conceal the existence of a lay-up credit. We do not believe there is any evidence to support this hypothesis. (See A.R.B., § VI.) Indeed, as we have explained, this was not even Textron's theory at trial. But even if there was *some* evidence to support Textron's conspiracy theory, the trial court, sitting "as an independent trier of fact" (*Neal v. Farmers Ins. Exchange, supra,* 21 Cal.3d at p. 933), properly could find that no conspiracy occurred.

The trial court's comments made clear it did not believe National Union was directly involved in any alleged coverup. Following the jury's finding that National Union acted with fraud, malice and oppression, the trial court remarked: "I think it's more likely that the jury found National Union in the soup here because of TRM. . . . " (R.T. p. 4814.) And, at the new trial hearing, the trial court indicated that, in its view, National Union's own wrongful conduct consisted of failing to make "an independent decision whether this policy covered Textron's interest quite apart from what Ko had done." (R.T. p. 4990.)

In *BMW of North America, Inc. v. Gore, supra,* 517 U.S. 559 [134 L.Ed.2d 809, 116 S.Ct. 1589], the United States Supreme Court held that "the degree of reprehensibility of the defendant's conduct" is "[p]erhaps the most important indicium of the reasonableness of a punitive damage award." (*Id.* at p. ___ [116 S.Ct. at p. 1599].) If National

Union did not conspire with TRM to manufacture documents and instead was guilty only of what the trial court believed was an unreasonable interpretation of its policy, "the degree of reprehensibility of [its] conduct" was low if not non-existent. Because the trial court's conclusion that there was no conspiracy between National Union and TRM was supported by substantial evidence, it did not abuse its discretion in holding that the jury's $10 million punitive damage award was excessive.

* * *

4th Civil No. G020323

IN THE COURT OF APPEAL OF THE
STATE OF CALIFORNIA
FOURTH APPELLATE DISTRICT
DIVISION THREE

TEXTRON FINANCIAL CORPORATION,

Plaintiff, Respondent, Cross-Appellant (and Separate Appellant),

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA, et al.

Defendants and Appellants.

On Appeal From The Superior Court of Orange County
Hon. Raymond J. Ikola
Case No. 734096

TEXTRON'S REPLY BRIEF ON ITS CROSS-APPEAL

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VI. BMW V. GORE DID NOT MANDATE THE TRIAL COURT'S DRASTIC REDUCTION OF PUNITIVE DAMAGES

National Union's arguments praising the trial court's reduction of punitive damages demonstrate a key reason why the jury's $10,000,000 punitive damage award was required. National Union's relentless attacks against Textron, in the face of extraordinary insurer misconduct, convinced the jury that nothing less would get National Union's attention.

National Union again devotes much attention to the United States Supreme Court decision of *BMW of North America v. Gore* (1996) 517 U.S. 559, 134 L.Ed.2d 809, 116 S.Ct. 1589. But there are several reasons why *BMW* did not necessitate the trial court's drastic reduction of the jury's verdict.

First, *BMW* did not overrule cases that *affirm* similar punitive damages awards in similar situations. The *BMW* Court stated:

> "[T]he record in this case discloses no deliberate false statements, acts of affirmative misconduct, or concealment of evidence of improper motive, such as were present in *Haslip* and *TXO*. . . . [T]he omission of a material fact may be less reprehensible than a deliberate false statement. . . . " (116 S.Ct. at 1601.)

Unlike *BMW*, this case included affirmative and deliberate false statements, concealment (and even destruction) of evidence, and a bitter attack on a policyholder by an insurance company that had a duty to treat the policyholder fairly and with utmost good faith.

In distinguishing affirmative misconduct cases, the *BMW* Court noted that BMW's conduct was perfectly legal in many states. *Id.* at 1594. National Union cannot argue that insurance fraud is legal in even one state.

Second, the trial court's use of *BMW* to reduce the jury's punitive damages verdict was erroneous because *BMW*'s focus concerned "fair notice" of "the severity of the penalty that States may impose." 116 S.Ct. at 1598. The trial court erred when it used *BMW* to drastically reduce the jury's verdict even though it expressly found that National Union had fair notice that its conduct could result in imposition of substantial punitive damages. (C.T. 4828.)

Finally, California's interest in deterring state-licensed insurers from committing insurance fraud against policyholders is significantly greater, and much more urgent, than Alabama's interest in deterring car manufacturers from failing to disclose that they repaired a car's paint job before it was sold. *BMW* recognized that there will be "different classes of cases." *Id.* at 1595. But, in this case, the trial court reduced the jury's verdict without considering that *BMW* and this case represented two cases in very different classes, and without considering that the state interests at issue differed dramatically.[13]

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[13] This explains why only eight days after it decided *BMW*, the Supreme Court denied certiorari to review a $14 million punitive damages award rendered against an insurance company under California law. See *Chemstar, Inc. v. Liberty Mut. Ins. Co.* (9th Cir. 1994) 1994 Westlaw 650018, *cert. denied*, May 28, 1996, 134 L.Ed.2d 948.

BMW expressly held that it is only when an award is "grossly excessive" in relation to state interests the award will promote that it "enter[s] the zone of arbitrariness that violates the due process clause of the Due Process Clause of the Fourteenth Amendment." *Id.* at 1594. In this case, the trial court's exclusive focus on the ratio of punitive to compensatory damages could not justify the conclusion that the jury's award was "grossly excessive," particularly in view of the reprehsnible [sic] nature of the misconduct toward Textron.

National Union strings together a long list of cases involving reduced punitive damages awards, as if the issue should be decided by the number of cases a party can cite. However, those cases have little similarity to this case. For example, several reduced the amount of punitive damages because the award was excessive in comparison to *the defendant's ability to pay*. See, e.g., *Kim v. Dial Service Int'l, Inc.* (S.D.N.Y. 1997) 1997 U.S.Dist. LEXIS 12544, at page 15 (*47) (supervisor guilty of harassment did not have a large net income, and the corporate employer was losing money).

In this case, the defendant's $3.7 billion net worth was an important factor supporting the jury's award of punitive damages. While a large punitive damages award may be subject to reduction when the defendant has limited means, a larger award is *required* when the defendant is wealthy, or else it will have relatively little deterrent effect. *Stevens v. Owens-Corning Fiberglass Corp.* (1996) 49 Cal.App.4th 1645, 1658 ("The wealthier the wrongdoer, the larger the punitive damage award must be to meet the goals of punishment and deterrence.").

And like *BMW*, many cases National Union lists involved conduct that was little more than negligent. For example, in *Apache Corp. v. Leo Moore* (1997) 1997 Tex. App. LEXIS 4031, at page 5 (*7) the Texas court reduced the award pursuant to a Texas statute limiting the ratio of compensatory and punitive damages in *negligence* cases. See also *Leab v. Cincinnati Ins. Co.* (E.D.Pa. 1997) 1997 U.S. Dist. LEXIS 8868, at page 14 (*40) (punitive damages based on delay, even though the insurer's position was correct, and the insurer paid the amount due under the policy).

National Union does not cite any case where a court reduced a substantial punitive damages award under circumstances similar to this case. The reprehensible nature of the conduct, and California's strong interest in deterring similar abuses by National Union and other California insurers, justified the jury's $10 million punitive damages assessment.

* * *

G020323

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DIVISION THREE

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Plaintiff and Respondent,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Defendant and Appellant.

PETITION FOR REHEARING

Defendant and appellant National Union Fire Insurance Company of Pittsburgh,Pennsylvania, respectfully petitions for rehearing following the court's January 29, 2001 opinion. The petition is made on the ground the court omitted and misstated material facts.[1]

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[1] Rule 29(b), California Rules of Court, provides: "As a matter of policy, on petition for review the Supreme Court normally will not consider: . . . (2) any issue or any material fact that was omitted from or misstated in the opinion of the Court of Appeal, unless the omission or misstatement was called to the attention of the Court of Appeal in a petition for rehearing."

Specifically:

1. The opinion omits the fact that the general agency agreement between National Union and TRM International (TRM) provided that TRM had "no authority to investigate, defend, approve or deny any claim made against [National Union] . . . and . . . no authority to assign an adjuster or attorney to investigate or defend any claims" (Ex. 170, ¶ 8.)

2. The opinion states that "the basis of the denial [of Textron's claim] was that Ko deleted the bus from the policy before the accident, and TRM and AIAC concluded National Union's policy did not obligate it to give [Textron] advance notice of the deletion." (Typewritten Opn., p. 4.) This statement inaccurately attributes to TRM a role in the denial of coverage. TRM did not advise National Union and AIAC that Textron was not entitled to advance notice of the deletion. Rather, TRM simply advised National Union and AIAC of the facts – that the bus had been deleted. AIAC and National Union made the decision that the policy did not entitle Textron to advance notice of the deletion. (See, e.g., R.T. p. 4076 [testimony of National Union underwriter John Lavin] Q: "And did [Ella Quinlan of AIAC] discuss with you and Mr. Spangenberg [of TRM] what the consequences of that time line was in terms of coverage for the accident to the bus?" A: "Yes. She discussed it. But I didn't offer any answer for it. I'm not sure Tom [Spangenberg] did. He just matter of factly told her the time line and, I guess, she listened."]; See also Exs. 58, 59, 229, 230; R.T. pp. 2253, 2324, 2328-2330, 2809, 3055-3056.)

3. The opinion states: "[W]hen Ko submitted a claim on the bus, TRM . . . advised AIAC to deny the claim. Furthermore, TRM's president was in contact with both AIAC and senior management of the division handling National Union's bus program when [Textron's] claim was being considered, and participated in the ultimate decision to deny it." (Typewritten Opn., p. 20.) This statement once again inaccurately attributes to TRM a role in the denial of coverage. TRM merely advised AIAC and National Union that the bus had been deleted from the policy before the January 7, 1993 accident. It did not advise AIAC or National Union that as a consequence either Ko's or Textron's claim should be denied. Those coverage decisions were made by AIAC and National Union. (See ¶ 2, *ante;* see also Ex. 505, p. 10; R.T. pp. 1426-1429.)

4. The opinion states that "[o]n February 4, TRM sent AIAC a notice verifying coverage for the bus" (Typewritten Opn., p. 4), that "AIAC directed its employees to contact TRM when seeking coverage verification" (Typewritten Opn., p. 20), and that "TRM initially issued a coverage determination. . . . (*Ibid.*) These statements fail to fully describe TRM's function when it was asked to provide a coverage verification. Upon receiving a request for a coverage verification from AIAC, a low level TRM employee would simply review the policy's schedule of vehicles and determine whether the vehicle in question was listed. (R.T. pp. 1644-1645.) Coverage "determinations," e.g., how policy provisions should be interpreted, or whether a claim should be paid, were made by AIAC, not TRM. (Exh. 170, ¶ 8.)

5. The opinion states that "on December 1, TRM reinstated the policy effective as of November 27. The bus encumbered by [Textron's] security interest was one of the vehicles Ko intended to use. [Textron] did not receive notice of the policy reinstatement with the endorsement which reflected Ko's business received a premium credit due to the vehicle's non-use. National Union claimed it sent a copy of this endorsement to plaintiff, but plaintiff denied receiving it." (Typewritten Opn., p. 3.) This statement is inaccurate and misleading for two reasons. First, the reinstatement notice and the endorsement were two separate documents. The reinstatement notice was issued by TRM on December 2, 1992 (Ex. 20) and the endorsement was prepared by TRM on February 11, 1993 (Ex. 38). Second, and more significantly, National Union never claimed that it sent either document to Textron. Rather, TRM claimed to have mailed a copy of the endorsement to Textron. (Ex. 78, p. 42.)

Accordingly, rehearing should be granted or the opinion corrected as indicated.

Dated: February 13, 2001

Respectfully submitted,

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COURT OF APPEAL – STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORP.,
Plaintiff and Respondent,

v.

NATIONAL UNION FIRE INSURANCE CO.,
Defendant and Appellant.

G020323

Sup. Ct. No. 734096

ORDER

(Filed Feb. 27, 2001)

The petition for rehearing is DENIED.

/s/ Rylaarsdam, J.
RYLAARSDAM, J.

WE CONCUR:

/s/ Sills, P.J.
SILLS, P.J.

/s/ O'Leary, J.
O'LEARY, J.

G020323

IN THE COURT OF APPEAL
OF THE STATE OF CALIFORNIA
FOURTH APPELLATE DISTRICT
DIVISION THREE

TEXTRON FINANCIAL CORPORATION
a Delaware Corporation,

Plaintiff and Respondent,

vs.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Defendant and Appellant.

MOTION TO STAY ISSUANCE OF REMITTITUR PENDING PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES SUPREME COURT

Pursuant rule 25(c), California Rules of Court, defendant and appellant National Union Fire Insurance Company of Pittsburgh, Pennsylvania (National Union) hereby moves for an order staying issuance of the remittitur pending disposition by the United States Supreme Court of a petition for writ of certiorari. This motion is based on the accompanying memorandum of points and

authorities and the accompanying declaration of Peter Abrahams.

Respectfully submitted,

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MEMORANDUM OF POINTS AND AUTHORITIES

ISSUANCE OF THE REMITTITUR SHOULD BE STAYED TO PERMIT NATIONAL UNION TO SEEK REVIEW BY THE UNITED STATES SUPREME COURT.

In this case, National Union appealed from a judgment for $165,414.40 in compensatory damages and $1.7 million in punitive damages in favor of plaintiff and respondent Textron Financial Corporation (Textron). On January 29, 2001, this court affirmed that judgment. National Union's petition for review was denied by the California Supreme Court on May 2, 2001. (No. S095924.) The judgment will therefore become enforceable upon

filing of the remittitur. (See Code Civ. Proc., § 917.1, subd. (b).)

Under normal circumstances, the clerk of the Court of Appeal issues the remittitur "upon expiration of the period during which review in the Supreme Court may be determined. . . . " (Cal. Rules of Court, rule 25(a).) However, "[a] reviewing court, for good cause, may stay the issuance of a remittitur for a reasonable period." (Cal. Rules of Court, rule 25(c).) The effect of such a stay is "to delay the date when jurisdiction would normally be revested in the lower court for enforcement of the judgment. . . . " (9 Witkin, Cal. Proc. (4th ed. 1997) Appeal, § 735, p. 764.) "The main reason [to stay issuance of a remittitur] is to allow an opportunity for further review in the United States Supreme Court." (*Ibid.;* see also *Stevens Drilling co. v. Superior Court* (1936) 16 Cal.App.2d 435 [stay until United States Supreme Court passes on petition]; *Matthews v. Superior Court* (1989) 209 Cal.App.3d 155, 161, fn. 4; *Rosenthal v. Wilner* (1988) 197 Cal.App.3d 1327, 1333.)

There is good cause to stay issuance of the remittitur in this case because National Union should have the opportunity to petition the United States Supreme Court for certiorari on an issue presently pending before that court. In its petition for review in the California Supreme Court, National Union raised the issue whether this court satisfied its duty under the Due Process Clause of the Fourteenth Amendment to the United States Constitution to independently review the punitive damage award by stating the $1.7 million award was not excessive because the conduct in question was "reprehensible" and National Union was wealthy. We argued that this court

was required by the federal Due Process Clause to independently review the punitive damage award for excessiveness in light of the three "guideposts" delineated by the United States Supreme Court in *BMW of North America, Inc. v. Gore* (1996) 517 U.S. 599: The *degree* of reprehensibility of the conduct, the ratio of punitive damages to the actual harm inflicted on the plaintiff, and the civil or criminal penalties that could be imposed for comparable misconduct. (*Id.* at pp. 574-584.)

In *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.* (No. 99-2035, cert. granted October 10, 2000, oral argument held February 26, 2001), the issue presented is "What is the standard of review of a trial court's ruling on a challenge to the constitutionality of a punitive damage award?" Because of the similarity of issues, National Union believes it is likely the United States Supreme Court will act favorably upon a petition for certiorari in this case.

There will be no prejudice to Textron from issuance of a stay. National Union has posted an undertaking in the full amount required by statute to stay enforcement of the judgment which will remain in force during the pendency of any proceedings before the United States Supreme Court, and the judgment will earn interest at the statutory rate until the judgment is paid. Thus, Textron

will be fully secured and confronts no risk of loss created by the relief requested herein.

Respectfully submitted,

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Case No.

G020323

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT, DIVISION THREE

TEXTRON FINANCIAL CORPORATION,

Plaintiff and Appellant,

v.

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA et al.,

Defendants and Appellants.

OPPOSITION TO MOTION TO STAY ISSUANCE OF REMITTITUR

Appeal from a Judgment of the
Superior Court of Orange County
Raymond J. Ikola, Judge
(Super. Ct. No. 734096)

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INTRODUCTION

National Union's motion to stay issuance of the remittitur should be summarily denied. National Union has not even tried to address the criteria necessary to justify a stay. To warrant a possible stay of issuance of the remittitur, National Union must show: (1) a reasonable probability that four United States Supreme Court Justices would vote to grant certiorari; (2) a significant possibility that the United States Supreme Court would reverse the existing judgment; and (3) a likelihood of irreparable harm if issuance of the remittitur was not stayed.

In addition, the "good cause" requirement means that a stay cannot be justified without "a showing of some *extraordinary reason* for retaining appellate court jurisdiction and further delaying lower court proceedings on the judgment. . . . " (Eisenberg, Horvitz & Wiener, Cal. Practice Guide: Civil Appeals & Writs (TRG 2000) § 14:30, italics in original.)

National Union's motion does not address these issues. Instead, National Union simply says it wants to file a petition for certiorari with the United States Supreme Court. Because National Union's motion is wholly inadequate, Textron urges this court to deny National Union's motion and issue the remittitur.

ARGUMENT

I

National Union Has Failed to Establish a Reasonable Probability That Four Supreme Court Justices Would Vote to Grant Certiorari.

The first requirement for a party seeking a stay of a judgment in these circumstances is a showing of reasonable probability that four justices would vote to grant certiorari. (See, e.g., *Packwood v. Senate Select Committee on Ethics* (1994) 510 U.S. 1319, 1319.)

Instead of making an effort to satisfy this requirement, National Union simply says one case that was already argued raised a "similar" issue. National Union does not explain the facts or circumstances of the other case that create this alleged "similarity" of issues. Nor does National Union explain why an unrelated case would generate a grant of certiorari in this case.

While National Union now seems to be arguing that this court's written opinion was not long enough (and that it did not specifically refute each and every aspect of the arguments the parties raised in several hundred pages of briefing), National Union waived this argument by failing to raise it in the petition for rehearing it filed on February 14, 2001. (See Cal. Rules of Court, rule 29(b)(2).)

In addition, National Union raised the same invalid argument it wants to make in the United States Supreme Court in its petition for review to the California Supreme Court. Not surprisingly, our Supreme Court denied National Union's petition, and there is no reason to

believe another court would treat National Union's improper argument any differently.

II

National Union Has Failed to Establish Any Likelihood That the Judgment Would Be Reversed.

A second requirement for any party seeking stay pending a possible filing of a petition for certiorari is the showing of a "significant possibility that the Court would reverse the judgment below." (*Packwood, supra,* 510 U.S. at p. 1319; see also *Graves v. Barnes* (1972) 405 U.S. 1201, 1203-1204.)

National Union's motion seem to imply (but does not actually say) that the case of *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.* (No. 99-2035) could control the outcome of this case. It cannot.

The question presented in *Cooper* is: "What is the standard of review of a trial court's ruling on a challenge to the unconstitutionality of a punitive damage award?" (*Cooper,* brief for petitioner at p. i; copy of brief attached as ex. A.)[1] This issue arose because the Ninth Circuit, in affirming a trial court's ruling, held that "the district court did not abuse its discretion in declining to reduce the amount of punitive damages." (*Leatherman Tool Group, Inc. v. Cooper Industries, Inc.* (9th Cir. Dec. 17, 1999, Nos. 98-35147, 98-35415) 1999 U.S. App. Lexis 33657, at *5; copy attached as ex. B.)

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[1] The document is also available at http://supreme.lp.findlaw.com/supreme court/docket/2000/febdocket.html #9902035.

The present case is nothing like *Cooper*. Here, this court did not apply the "abuse of discretion" standard; rather, it independently concluded that "the record reflects the present award is permissible under both state and federal law." (Typed opn. at p. 23.) In other words, this court applied the de novo standard that petitioner is advancing in *Cooper*. (*See Cooper*, brief for petitioner at pp. 12-23.)

Cooper will have no effect on this case. If the United States Supreme Court adopts the de novo standard, this court has already complied with it. If the high court adopts the abuse of discretion standard, National Union received a more thorough review than that to which it was entitled, and cannot complain. No matter how *Cooper* is decided, the present case will not be reversed.

National Union also forgets that the trial judge in this case painstakingly reviewed its constitutional arguments and then dramatically reduced the jury's punitive damages verdict. (C.T. 4824-4829.) The trial court reduced the punitive damages verdict by a full 83 percent despite its finding that National Union "does not contend, nor can it, that it did not have fair notice that the breach of the covenant of good faith and fair dealing could result in the imposition of substantial punitive damages under the common law." (C.T. 4828.)

National Union failed to convince the jury that its witnesses were telling the truth, it failed to convince the trial court that it had not engaged in serious wrongdoing, it failed to convince this Court that the record did not support the award, and it failed to convince the California Supreme Court to hear this case. There is no reason to

believe the United States Supreme Court would view this case any differently.

For this reason also, National Union's motion should be denied.

III

National Union Has Failed to Establish Irreparable Harm.

To justify a stay, National Union is also required to demonstrate "a likelihood of irreparable harm, assuming the correctness of [National Union's] position, if the judgment is not stayed." (*Packwood, supra,* 510 U.S. at p. 1319.)

Rather than try to establish irreparable harm, National Union blithely says Textron will not suffer any prejudice from issuance of a stay. (Motion at p. 4.) National Union's argument shows a serious misunderstanding of the showing that would have been required to justify any eleventh hour stay. To justify a stay, National Union would have to show that it would be irreparably harmed in the absence of a stay.

National Union has not attempted to establish any irreparable harm because it cannot do so. National Union owes a money judgment, pure and simple. Even in the unlikely event that the United States Supreme Court would grant certiorari *and* reverse the judgment, National Union has not demonstrated that Textron would defy court orders and not return the money. National Union has not and cannot show irreparable harm. For this additional reason, National Union's motion should be denied.

CONCLUSION

National Union's motion fails to address, much less establish, the criteria that would be needed to justify consideration of a stay request.

National Union is not entitled to a stay or any further delay. Textron respectfully urges this court to deny National Union's motion and issue the remittitur forthwith.

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PROOF OF SERVICE

(Code Civ. Proc., § 1013a, subd. (3))

I am employed in the county of Orange, State of California. I am over the age of 18 years and not a party to this action; my business address is 535 Anton Boulevard, Suite 800, Costa Mesa, California 92626.

On May 9, 2001, I served the Opposition to Motion to Stay Issuance of Remittitur on the interested parties in this action by placing true copies enclosed in sealed envelopes addressed as follows:

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(Attys. for National Union)

Court of Appeal
Fourth District, Division Three
925 N. Spurgeon Street
Santa Ana, CA 92701
(Original and three copies
by hand delivery)

R. Gaylord Smith
LEWIS, D'AMATO ET AL.
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(Attys. for National Union)

I am familiar with the business practice at my place of business for collection and processing of correspondence for mailing with the United States Postal Service. Correspondence so collected and processed is deposited with the United States Postal Service that same day in the ordinary course of business.

I declare under the penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on May 9, 2001, at Costa Mesa, California.

_____
Raquel Moreno

IN THE

COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

TEXTRON FINANCIAL CORPORATION, Plaintiff and Appellant, v. NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA et al., Defendants and Appellants.	G020323 (Super. Ct. No. 734096) ORDER (Filed May 11, 2001)

Appellant National Union Fire Insurance Company of Pittsburgh, Pennsylvania, filed a motion to stay issuance of the remittitur to allow it time to file a petition for a writ of certiorari with the United States Supreme Court. (See Cal. Rules of Court, rule 25(c).) Having read and considered the motion and opposition thereto, the motion is DENIED.

/s/ Sills, P.J.
SILLS, P.J.

STATUTORY PROVISIONS INVOLVED

California Rules of Court, Rule 29(b):

As a matter of policy, on petition for review the Supreme Court normally will not consider:

> (1) any issue that could have been but was not timely raised in the briefs filed in the Court of Appeal;
>
> (2) any issue or any material fact that was omitted from or misstated in the opinion of the Court of Appeal, unless the omission or misstatement was called to the attention of the Court of Appeal in a petition for rehearing. All other issues and facts may be presented in the petition for review without the necessity of filing a petition for rehearing.

California Civil Code § 3294, subdivisions (a) & (c):

(a) In an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice, the plaintiff in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant.

* * *

(c) As used in this section, the following definitions shall apply:

> (1) "Malice" means conduct which is intended by the defendant to cause injury to the plaintiff or despicable conduct which is carried on by the

defendant with a willful and conscious disregard of the rights or safety of others.

(2) "Oppression" means despicable conduct that subjects a person to cruel and unjust hardship in conscious disregard of that person's rights.

(3) "Fraud" means an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.

California Civil Code § 3295, subdivision (d):

(d) The court shall, on application of any defendant, preclude the admission of evidence of that defendant's profits or financial condition until after the trier of fact returns a verdict for plaintiff awarding actual damages and finds that a defendant is guilty of malice, oppression, or fraud in accordance with Section 3294. Evidence of profit and financial condition shall be admissible only as to the defendant or defendants found to be liable to the plaintiff and to be guilty of malice, oppression, or fraud. Evidence of profit and financial condition shall be presented to the same trier of fact that found for the plaintiff and found one or more defendants guilty of malice, oppression, or fraud.

California Civil Code § 3296:

(a) Whenever a judgment for punitive damages is entered against an insurer or health care service plan licensed pursuant to Chapter 22 (commencing with Section 1340) of Division 2 of the Health and Safety Code, the plaintiff in the action shall, within 10 days of entry of judgment, provide all of the following to the Commissioner of the Department of Insurance or the Director of the Department of Management Health Care, whichever commissioner has regulatory jurisdiction over the insurer or health care service plan:

(1) A copy of the judgment.

(2) A brief recitation of the facts of the case.

(3) Copies of relevant pleadings, as determined by the plaintiff.

(b) The willful failure to comply with this section may, at the discretion of the trial court, result in the imposition of sanctions against the plaintiff or his or her attorney.

(c) This section shall apply to all judgments entered on or after January 1, 1995.

(d) "Insurer," for purposes of this section, means any person or entity transacting any of the classes of insurance described in Chapter 1 (commencing with Section 100) of Part 1 of Division 1 of the Insurance Code.

California Penal Code § 550, subdivisions (b) & (c) (pertinent parts):

(b) It is unlawful to do, or to knowingly assist or conspire with any person to do, any of the following:

(1) Present or cause to be presented any written or oral statement as part of, or in support of or opposition to, a claim for payment or other benefit pursuant to an insurance policy, knowing that the statement contains any false or misleading information concerning any material fact.

(2) Prepare or make any written or oral statement that is intended to be presented to any insurer or any insurance claimant in connection with, or in support of or opposition to, any claim or payment or other benefit pursuant to an insurance policy, knowing that the statement contains any false or misleading information concerning any material fact.

(3) Conceal, or knowingly fail to disclose the occurrence of, an event that affects any person's initial or continued right to any insurance benefit or payment, or the amount of any benefit or payment to which the person is entitled.

* * *

(c)(3) Every person who violates paragraph (1), (2), (3) or (4) of subdivision (b) shall be punished by imprisonment in the state prison for two, three, or five years, or by a fine not exceeding fifty thousand dollars ($50,000), unless the value of the fraud exceeds fifty thousand dollars ($50,000), in which event the fine may not exceed double the value of the fraud, or by both that imprisonment and fine; or by imprisonment in a county jail not to exceed one year, or by a fine of not more than one thousand five

hundred dollars ($1,500), or by both that imprisonment and fine.

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15 U.S.C. § 1011:

Congress hereby declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

Supreme Court, U.S.
FILED
SEP 10 200
CLERK

(3)

No. 01-176

IN THE

Supreme Court of the United States

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

v.

TEXTRON FINANCIAL CORPORATION,

Respondent.

On Petition for a Writ of Certiorari to the Court of Appeal of California, Fourth Appellate District

REPLY BRIEF FOR PETITIONER

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9PP

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Rule:

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IN THE

Supreme Court of the United States

No. 01-176

NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PENNSYLVANIA,

Petitioner,

v.

TEXTRON FINANCIAL CORPORATION,

Respondent.

**On Petition for a Writ of Certiorari
to the Court of Appeal of California,
Fourth Appellate District**

REPLY BRIEF FOR PETITIONER

Before this Court decided *Cooper Industries, Inc.* v. *Leatherman Tool Group, Inc.*, 121 S. Ct. 1678 (2001), the California appellate courts regularly employed a permissive standard of review when examining the constitutionality of a punitive damages award. Applying that lenient standard in this case, the California Court of Appeal rejected petitioner National Union's Fourteenth Amendment challenge to a punitive damages award amounting to over twenty times compensatory damages, affirming the judgment after declaring that it was "presumed to be correct" and reviewing the record "most favorably to the judgment." Pet. App. 24a. National Union petitioned the Supreme Court of California

for review of the Court of Appeal's ruling, explaining that the intermediate court should have engaged in an independent review of its constitutional claim, but the court denied National Union's petition without comment. *Id.* 43a. Twelve days after that, this Court issued *Cooper Industries*, holding that appellate courts "should apply a *de novo* standard of review when passing on district courts' determinations of the constitutionality of punitive damages awards." 121 S. Ct. at 1685-86.

In light of *Cooper Industries*, it is clear that the Court of Appeal applied the wrong standard of review. This Court recognized as much when it granted certiorari in a nearly identical case, vacated the Court of Appeal's decision, and returned the case to that court for further consideration. *San Paolo U.S. Holding Co.* v. *Simon*, 121 S. Ct. 2190 (2001). As it did there, this Court should grant certiorari, vacate the decision of the California Court of Appeal, and return this case to that court for proper consideration in light of *Cooper Industries*.

1. Respondent argues that National Union waived the right to seek further review of the Court of Appeal's constitutional ruling when it did not seek rehearing on that aspect of the court's decision. That is wrong. Rule 29 of the California Rules of Court states that a party need not seek rehearing in the Court of Appeal to preserve an issue for review in the California Supreme Court unless the Court of Appeal has "omitted * * * or misstated" an "issue or material fact." Cal. R. Ct. 29(b)(2); *see Torres* v. *Parkhouse Tire Serv.*, 2001 WL 987596, at *1 n.1 (Cal. Aug. 30, 2001) (because petitioner had not sought correction of factual error on petition for rehearing, California Supreme Court would not consider factual dispute on appeal); *Sweatman* v. *Department of Veterans Affairs*, 18 P.3d 29, 33 n.1 (Cal. 2001) (where Court of Appeal had neglected to address issue of exhaustion of remedies and petitioner had not sought rehearing to correct omission, California Supreme Court would not

consider issue). Aside from such omissions or misstatements, "[a]ll other issues and facts may be presented in the petition for review without the necessity of filing a petition for rehearing." Cal. R. Ct. 29(b)(2).

Adhering to Rule 29(b)(2), National Union sought rehearing of certain aspects of the Court of Appeal's decision, arguing that the court had omitted or misstated several facts material to its decision. *See* Opp. App. 50-53. National Union did not seek rehearing of the Court of Appeal's decision affirming the trial court's punitive damage award, because it would have been inappropriate—not to mention unavailing—for National Union to challenge what was then the settled standard of review of punitive damage awards by seeking rehearing in the intermediate court.

Before *Cooper Industries* was decided, the California Supreme Court had repeatedly held that a punitive damages award was to be reviewed "in a light most favorable to the judgment," to determine whether the jury's award was the result of "passion or prejudice." *Neal* v. *Farmers Ins. Exchange*, 582 P.2d 980, 986 (Cal. 1978); *Bertero* v. *National General Corp.*, 529 P.2d 608, 624 n.12 (Cal. 1974). The Court of Appeal had consistently applied that lenient standard, up to and including this case. *See* Pet. for Cert. 11-13 (citing cases); Pet. App. 24a. The intermediate court was not in a position to change the settled standard of review, and National Union's arguments against that standard were properly directed to the California Supreme Court in the first instance. *See People* v. *Birks*, 960 P.2d 1073, 1077 n.6 (Cal. 1998) (because "[t]he Court of Appeal must follow, and has no authority to overrule, the decisions of this Court," respondent's argument that petitioner should have raised, in Court of Appeal, an argument requiring the overruling of California Supreme Court precedent was "specious"); *Moradi-Shalal* v. *Fireman's Fund Ins. Cos.*, 758 P.2d 58, 60 n.1 (Cal. 1988) (rejecting argument that issue should have been raised in Court of Appeal; "clearly it was pointless for the defendant to

ask either the trial or the appellate court to overrule one of our decisions").

2. Textron next argues that National Union "invited" the Court of Appeal to apply a lenient standard of review when examining the constitutionality of the punitive damages award because it "urged the court [of appeal] to apply an abuse of discretion standard." Opp. 2, 11, 14, 15. Textron is purposely conflating two separate arguments advanced in two separate briefs in response to two separate issues.

In National Union's opening brief on appeal, it urged the Court of Appeal to review the punitive damage award and reject it as unconstitutionally excessive. Under *Cooper Industries*, that constitutional question should have been reviewed *de novo*. 121 S. Ct. at 1683. In Textron's brief on its cross-appeal, Textron argued that the trial court should not have ordered a remittitur at all. Responding to Textron's argument in its combined opposition and reply brief—and after again pressing its point that the $1.7 million award violated the Fourteenth Amendment—National Union argued that "[a]ssuming punitive damages are proper at all and that the $1.7 million award is not excessive, the trial court's remittitur should be affirmed."[1] That separate issue—whether the trial court properly ordered a remittitur—is reviewed on appeal for abuse of discretion. Cal. Civ. Proc. Code § 662.5(b) (West 2001); *Wallis* v. *Farmers' Group, Inc.*, 269 Cal. Rptr. 299, 312 (Cal. Ct. App. 1990). National Union articulated that standard in response to Textron's cross-appeal, *not* in its own constitutional challenge to the hefty punitive damages judgment remaining after remittitur. *See* Opp. App. 40, 42.

3. Having exhausted its technical objections, Textron resorts to obfuscation. First, it recharacterizes National

[1] Combined Appellant's Reply Brief, Cross-Respondent's Brief, and Respondent's Brief on Separate Appeal at 50; *see id.* at 53 (same).

Union's petition as having argued that the Court of Appeal "ignored federal punitive damages standards." Opp. 15; *id.* at 23 ("National Union's petition is based on the erroneous assumption that the Court of Appeal never evaluated federal law punitive damages standards"). From this flawed starting point, Textron launches into a lengthy—and completely irrelevant—discussion of state and federal "guideposts" for review of punitive damages awards, *id.* at 16-21, explaining at length that the Court of Appeal "appreciate[d] the differences between federal and state punitive damages law." *Id.* at 20.

National Union did not petition for certiorari on the ground that the Court of Appeal "ignored federal punitive damages standards." *Id.* at 15. It sought certiorari because when the Court of Appeal evaluated those federal guideposts, it applied a standard of review this Court has found to be too lax, stating that the punitive award was "*presumed to be correct*" and would be reversed "only if the record, *viewed most favorably to the judgment*, reflects [that] the award is the result of passion or prejudice." Pet. App. 24a (emphases added). *That* is the issue in this case, and Textron offers no substantive response to it. Indeed, in its thirty-page opposition, Textron never mentions the lenient standard of review the Court of Appeal employed in examining the punitive award. Rather than confronting that unambiguous text, Textron repeats the mantra (four times on page 21 alone) that the Court of Appeal "independently" considered the constitutionality of that award. *See, e.g.*, Opp. 1, 15, 21, 22, 23, 30. Repeating something does not make it so. The Court of Appeal examined the constitutionality of the punitive damages award by first *presuming* the punitive damages determination to be correct, viewing the record "most favorably to the judgment," and immediately after that, discussing the *BMW* standards. Pet. App. 24a. The Court of Appeal did the same thing in *San Paolo*, the decision this Court vacated and

remanded after *Cooper Industries*. *See* Pet. App. (No. 00-1457) at A-28, A-31.

4. Textron's remaining arguments are also meritless. It argues that the $1.7 million punitive damages award was proper under any standard of review because National Union's conduct was reprehensible. Opp. 24-27. But the Court of Appeal never addressed that argument. It concluded that National Union was responsible for the actions of its affiliate, and it specifically declined to address whether National Union's own actions warranted the punitive award. *See* Pet. App. 21a (declining to consider National Union's argument on "the insufficiency of the evidence based on its own conduct"). If this Court vacates the judgment and remands, the Court of Appeal can address Textron's arguments when it independently considers the constitutional propriety of a punitive award against National Union—under the correct standard of review. Textron also suggests that the original jury verdict should be reinstated. Opp. 27-29. It did not petition for certiorari on that issue.

5. Most tellingly, only in passing does Textron acknowledge *San Paolo U.S. Holding Co.* v. *Simon*, in which this Court granted certiorari, vacated the decision of the Court of Appeal applying a deferential standard of review on a constitutional challenge to a punitive damage award (for the same amount at issue here, no less), and remanded for consideration in light of *Cooper Industries*. 121 S. Ct. 2190 (2001). Textron attempts to distinguish *San Paolo* by explaining that the Court of Appeal in *San Paolo* "fail[ed] to appreciate the differences between federal and state punitive damages law," as if that somehow precipitated the GVR in that case. Opp. 20. Not so. The Court of Appeal in *San Paolo* articulated the *BMW* standards; but just as it did here, it applied a too-lenient standard of review when it examined the constitutionality of the punitive damage award. Pet. App. (No. 00-1457) A27-28, A31. That is why the judgment in that case was appropriate for further consideration after

Cooper Industries. So too here. This Court should follow the same course it took in *San Paolo*: grant certiorari, vacate, and remand for consideration in light of *Cooper Industries*.

CONCLUSION

For the foregoing reasons, and for those in the petition, the petition should be granted, the judgment below vacated, and the case remanded for further consideration in light of *Cooper Industries* v. *Leatherman Tool Group*.

Respectfully submitted,

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